Working Paper Series

GOVERNMENT PENSIONS AND TRUE 'REFORM' - BAND-AIDS OR MAJOR SURGERY?

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Prepared for: Ontario Economic Council
October, 1983

Ontario Economic Council
Toronto,Ontario

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SUMMARY

We fancy that the largest subsidies go to those most in need: for Senior Canadians, the facts are often otherwise. High-income Senior Canadians are often considerably subsidised, sometimes being given more dollars of subsidy per month than those with lower incomes. Also, as between two individual Senior Canadians at about the same income level, the one earning slightly less may have substantially more spendable income than the one earning slightly more.

We fancy that the taxation of income in Canada is progressive: for Senior Canadians, the facts are otherwise. More than a few Senior Canadians are in a 100% income tax bracket. Even though they earn more, by working or by saving, their net income to spend is not thereby increased at all. That's 100% taxation. In general, the Senior Canadians with the lowest incomes are in the highest tax brackets.

We may fancy that Government pensions have been carefully designed, and are now administered efficiently: some of the facts are otherwise. Some of the benefits promised by Parliament to Senior Canadians are not being paid out. Other senior Canadians with fluctuating incomes find themselves snared in excessive red tape. Government pensions have some needless administrative costs.

Surely the majority of Canadians, at all ages, favour the largest monthly dollar subsidies being paid to those Senior Canadians with the lowest incomes, and with subsidies then steadily less and less for those with higher and higher incomes? Surely a majority of Canadians, at all ages, favour taxation of the incomes of Senior Canadians being progressive, for example, low-income Senior Canadians having the lowest tax brackets?

From the same totals of Government pension monies as are now being collected from taxpayers, we can obtain 'better value'. Different patterns

from those now in place in Canada have already been developed. Canadians should be given an opportunity for comparison shopping among the alternatives.

If a 'better buy' is adopted, then it will be more effective and more equitable for Senior Canadians. Also, administration will be more economical, with less overhead costs for Canadian taxpayers to bear.

1
THE CPP/QPP AND 'UPSIDE-DOWN WINDFALLS'

The Canadian Labour Congress (the CLC) advocates that age retirement pensions under the Canada Pension Plan and under the Quebec Pension Plan (the CPP/QPP) be doubled, from 25% of covered pre-retirement earnings up to 50% of covered pre-retirement earnings.

Regarding such possible CPP/QPP expansion, the December 1982 federal Green Paper, 'Better Pensions for Canadians', states:

> 'Public plans have a number of advantages. They provide retirement benefits which are immediately vested, portable and normally fully indexed to the cost-of-living. An expansion of the public system could be implemented so that workers would receive significant benefits much sooner than the 30 or more years required with private sector expansion. All of this could be done with minimal additional administrative cost.'

It is as if the CLC and the authors of the Green Paper imagine the CPP/QPP to be fundamentally the same kind of animal as a negotiated employment pension plan, excepting only that the CPP/QPP have 'a number of advantages'. In fact, such is not the case.

Major differences

The truth is, the CPP/QPP are indeed very different from a typical flat benefit pension plan as commonly negotiated by a trade union, regarding the two vital design aspects of:

A. Past Service (see Chapter 2)

B. Benefit Formula (discussed below) and - as a direct result of the Benefit Formula coupled with the Contribution Formula - associated by-products, including: - subsidies, windfalls, not-paid-for generosity, e.g. as one trade union witness to the federal Task Force on Pension Reform phrased it, the 'Irish sweepstakes'.

Benefit formula

A typical flat benefit pension plan negotiated by a trade union pays equal benefits to any two persons with the same years of service at retirement. Such plans are not guilty of discrimination regarding any of the following cases:

- a woman vs. a man
- an older worker vs. a younger worker
- a lower-income worker vs. a higher-income worker.

In other words, the pension benefits under such plans are people-related.

The CPP/QPP do discriminate

By contrast, the CPP/QPP do indeed discriminate... usually against the financially weaker and needier person... and usually in favour of the financially stronger and less needy person.

As first published in the October 15, 1982 issue of 'Canadian Business Management Developments', and reproduced with the permission of Mr. J.N. Grace, Managing Editor, CCH Canadian Limited, Don Mills, Ontario, M3C 1Z5:

'CPP/QPP Miss the Target

'Curiously, despite elderly women being the greatest government pension concern, some non-business spokepersons in 'The Great Pension Debate' are pressing for increased benefits from the Canada Pension Plan and from the Quebec Pension Plan (CPP/QPP). This is curious and peculiar, because a majority of women aged 65 and over receive no monthly CPP/QPP cheques at all - neither so much as a cent of CPP/QPP retirement pension, nor even a cent of CPP/QPP survivor pension. They get nothing at all from the CPP/QPP.

'Even for the minority of female Senior Canadians who do receive something, in December 1981 the average monthly CPP cheque, for example, was $111. This $111 is a far cry from the commonly-quoted 1982 maximum monthly CPP/QPP retirement pension of $307.65. Further, compare that $111 female average against the corresponding male average monthly CPP cheque of $165. The female $111 is only 67 per cent of the male $165.

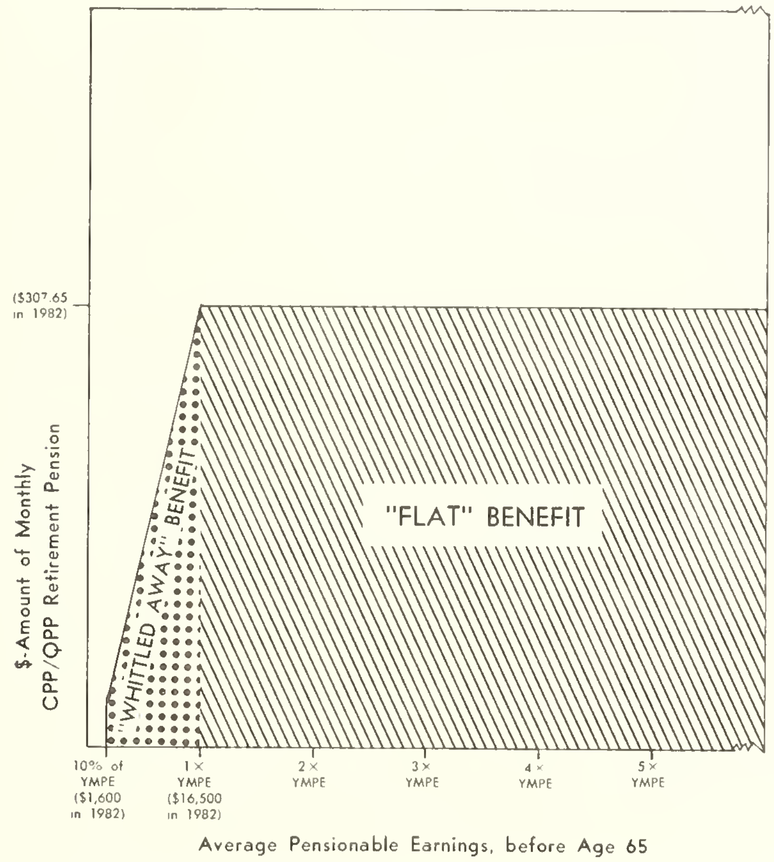
'In the light of even these few introductory realities, perhaps we should look a little further into pensions as a whole, before we leap into substantial CPP/QPP expansion. After all, as they now stand, the CPP/QPP already have a long-term cost of about 9 per cent of covered earnings. In addition, the GIS plus Old Age Security (OAS) are currently costing about $9 billion a year.

'Where do we start? Well, our new Constitution Act requires that government-run wealth sharing be directed mostly towards lower-income regions. Similarly, regarding government-run pensions, why not work along the same lines, directing help mostly towards those lower-income Senior Canadians who are most in need - especially elderly women? Unfortunately, the CPP/QPP retirement pension benefit formula is actually designed to avoid helping lower-income Senior Canadians. In essence, the CPP/QPP have a flat benefit formula, providing equal dollars a month for everyone retiring in the same year - except that the CPP/QPP formula is whittled away for those with below-average earnings before age 65.

'Thus, the CPP/QPP formula adds unto those who already have, but giveth less (or nothing!) to those who have less. This can be readily grasped from the chart below:

CHART 1

CPP/QPP RETIREMENT PENSION



'This whittling away of the lower end of the 'earnings-related' CPP/QPP retirement pension formula hits hardest those very senior Canadians most in current need, namely:

'1. Women. As above, CPP/QPP pensions are paid to considerably fewer female than male pensioners, and the average woman receives only about 67 per cent of the amount paid to the average man.

'2. Elderly Pensioners. On average, in December 1981:

Age Group	CPP Retirement Pension
65-70	$186
71-74	127
75-79	89
80 and over	54

'3. Lower-Income Earners. Those who earned below-average incomes before age 65 receive below-average CPP/QPP retirement pensions. In December 1981, out of 884,507 CPP retirement pensions in total, no less than 146,493 of them were under $50 a month!

'CPP/QPP 'Generosity' Misdirected

'You might be tempted to brush all this aside, by thinking as follows. 'Of course the winners are:

- men
- younger pensioners, and
- those who earned more before age 65.

After all, these winners get so much more out of the CPP/QPP simply because they paid in the most by way of CPP/QPP contributions. In other words, they and their employers have paid for their own CPP/QPP pensions - right?' As I will now explain, such thinking is - in one word - wrong!

'Those now receiving CPP/QPP pensions have paid for only a small, minority fraction of the cost of such pensions. By way of a first example, consider this from the March 1981 pension brief of the Canadian Chamber of Commerce (CC of C):

'Consider a 'round numbers' illustration for a homemaker. Suppose the CPP/QPP had permitted a homemaker to contribute in 1980. A homemaker then age 64, with a high-income husband who contributed $400 to the CPP/QPP for the year 1980 and who then retired, could then expect to receive $200 a year from the CPP/QPP during her expected 17-year retired lifetime. She would pay in $400 once, but would receive back 17 times $200, i.e. she would receive a total of $3,400. Thus, the high-income homemaker would receive $3,000 more than she paid in.'

'To see why the CPP/QPP are so 'generous' to above-average income earners, begin by recalling that the long-term CPP/QPP cost is about 9 per cent of covered earnings. Next, note that from 1966 up until now, the CPP/QPP have been levying contributions at a total rate of only 3.6 per cent of covered

earnings. This 3.6 per cent is 4/10 of the total long-term cost of 9 per cent.

'That is not the whole story, by any means. To qualify for a CPP/QPP retirement pension based on full-career service, a healthy man attaining age 18 now must contribute for just about 40 years. However, a special, concessionary 'past service' type of arrangement was built into the CPP/QPP, so that someone retiring at age 65 at the end of 1975 could receive a full pension, after only <u>ten years</u> of CPP/QPP contributions. Note that these ten years of contributions amount to merely <u>one-quarter</u> of the (approximately) 40 years of contributions required from today's 18 year-old man.

'Hence, the fraction of the CPP/QPP retirement pension actually paid for - in the case of the 65 year-old retiring at the end of 1975 - was only one-quarter of 4/10. That is, his CPP/QPP pension was about 1/10 paid for. In percentage terms, about 10 per cent was paid for. The balance of about 90 per cent was <u>not</u> paid for. Such 'generosity'! Even now, in 1982, by the same rough and ready (but reasonably indicative) figuring, less than 20 per cent of the CPP/QPP retirement pensions of those now retiring has been 'paid for'. More than 80 per cent has <u>not</u> been paid for. Again, 'generosity galore'!

'Already discussed above is the (typical and fairly representative) example of a high-income entitling someone aged 64 to pay $400 once to the CPP/QPP in 1980, and to be paid back $3,400 over the expected retired lifetime. By contributing in just one year, that person receives $3,000 of 'generosity'.

'Now for the lower-income counterpart, again from the CC of C March 1981 brief:

'By contrast, another 64 year-old homemaker just like the one above, except that her husband was earning close to the minimum wage, might only be allowed to contribute $200 in 1980. She would receive back 17 times only $100, i.e. a total of $1,700. This low-income homemaker would receive back $1,500 more than she paid into the CPP/QPP.'

'There you have it. Under the CPP/QPP, the lower your income, the less 'generosity' you receive!

'The essential points are these:

'1. For two pensioners of the same age, who contributed to the CPP/QPP for the same number of years, more dollars a month of <u>not</u>-paid-for 'generosity' go to the one who had the higher income before age 65.

'2. By the same token, fewer dollars a month of <u>not</u>-paid-for 'generosity' go to the one who had the lower income.

'Some people say, therefore, that the CPP/QPP earnings-related benefit formula results in 'upside-down generosity'. Others call the CPP/QPP, 'Robin Hood in reverse'. Where is the sense in all this?

<u>'OAS/GIS 'People-Related'</u>

'Not being earnings-related but, rather, being 'people-related', both OAS

and the GIS are generous in directions that are the opposite of the CPP/QPP. Under both OAS and the GIS, those with higher incomes before age 65 are net losers. The net gainers, under OAS/GIS, are those who had below-average incomes while working. Thus, the generosity of OAS/GIS to those in need - i.e. their 'benefit targeting' - makes sense for government-run pension plans.'

Remembering that this article used 'generosity' in the sense of not-paid-for subsidies or, if you prefer, not-paid-for windfalls, and referring just to such not-paid-for portions of the several benefits discussed, this same article continued as follows:

'Put in report card format, we have:

Is the 'Generosity' Directed Sensibly?

	(1) Less to men, more to women?	(2) Less to younger pensioners, more to older pensioners?	(3) Less to higher incomes, more to lower incomes?
CPP/QPP	No-reverse	No-reverse	No-reverse
OAS	Yes	Yes	Yes
GIS	Yes	Yes	Yes

'Thus, what really makes sense, in terms of facts and actual results now being achieved, is this: 'Leave the CPP/QPP the way they are now, without expanding their benefit formulas. It is the GIS that should be increased, to the extent needed.'

Further, as first published in the February 1, 1983 issue of 'Canadian Business Management Developments', and reproduced with the permission of Mr. J.N. Grace, Managing Editor, CCH Canadian Limited, Don Mills, Ontario M3C 1Z5:

'Silence of the Green Paper

'For addressing this CPP/QPP upside-down generosity, the Green Paper sets the stage well, thus: '...governments should ensure that individual Canadians are treated fairly' (emphasis added).

'Yet, the possible doubling of CPP/QPP retirement benefits is discussed, without any mention of such doubling having the inevitable consequence of massive upside-down generosity.

'A Simplified Example

'As a first simplified example of the upside-down generosity now already existing under the CPP/QPP, consider someone turning age 65 in January 1983 and who earned the CPP's YMPE (Year's Maximum Pensionable Earnings) from the starting year of 1966 up until the end of 1982.

'Table I shows that his contributions, in total for all years, equal $2,264.40. His 1983 CPP monthly retirement pension is $345.15. He, therefore, gets his total contributions back in less than seven months. Table I also shows a second person, who earned one-half of the YMPE, and who, therefore, contributed only $1,003.50. His 1983 CPP monthly retirement pension is $172.58. He also gets his total contributions back in less than seven months.

TABLE I

CPP Contributions Where ...

Year	1 x YMPE	½ x YMPE
1966	$ 79.20	$ 34.20
1967	79.20	34.20
1968	81.00	35.10
1969	82.80	36.00
1970	84.60	36.90
1971	86.40	37.80
1972	88.20	38.70
1973	90.00	39.60
1974	106.20	46.80
1975	120.60	54.00
1976	135.00	60.30
1977	151.20	67.50
1978	169.20	75.60
1979	190.80	85.50
1980	212.40	94.50
1981	239.40	107.10
1982	268.20	119.70
TOTALS	$2,264.40	$1,003.50

'Of course, for each person, his employer contributed an equal amount, as shown in Table II. Further, interest was earned within the CPP fund, which is shown (for simplicity) as doubling the total contributions.

TABLE II

Total CPP Contributions with (Approx.) Interest

		1 x YMPE	½ x YMPE
1.	Employee's total contributions	$2,264.20	$1,003.50
2.	Employer's total contributions	2,264.20	1,003.50
3.	Total	$4,528.40	$2,007.00
4.	Multiply x 2 to allow (approx.) for interest	x 2	x 2
5.	Total CPP contributions with (approx.) interest	$9,057.60	$4,014.00

'The average Canadian now turning age 65 can expected to live upwards of 15 years, i.e., upwards of 180 months. Using this (again, simplified) estimate, Table III gives a rough-but-faithful indication of the CPP's upside-down generosity.

TABLE III

CPP Upside-Down Generosity

		1 x YMPE	½ x YMPE
11.	1983 CPP monthly pension	$ 345.15	$ 172.58
12.	Expected lifetime, upwards of	180 months	180 months
13.	Expected total CPP pension (= Number 11 x Number 12), upwards of	$62,127.00	$31,064.40
14.	Less total CPP contributions with (approx.) interest (from Table II, Number 5)	-$9,057.60	-$4,014.00
15.	Expected generosity, upwards of	$53,069.40	$27,050.40

'Thus, even in this simplified example, it is clear that the not-paid-for generosity is at least ($53,069.40 less $27,050.40 =) $26,019 greater for the person who earned more while working. That is, indeed, upside-down generosity.

'Of course, the CPP/QPP as they now exist are here to stay, for as far ahead into the future as can be foreseen. However, nothing can alter the inevitability, as night follows day, of any increase in the 25 per cent CPP/QPP retirement benefit formula generating massive additional upside-down generosity. Told such facts by Canadian business, surely most Canadian voters will say 'No' to doubling the CPP/QPP? If most voters come to favour 'No', and one major political party also supports a 'No', then it could well be a political handicap for the other major political party to support a 'Yes' - whether federally, or in Quebec?'

1
SUMMARY

1. Under the CPP/QPP there is no fair play. Rather, there are winners and losers.
2. The CPP/QPP winners are:
   - by sex ... men
   - by age ... younger pensioners (born in 1911 or more recently)
   - by income ... higher-income earners.
3. The CPP/QPP losers are:
   - by sex ... women
   - by age ... older pensioners (especially those born 1895 or earlier)
   - by income ... lower-income earners.
4. Any increase in the 25 percent CPP/QPP retirement benefit formula will generate massive additional upside-down windfalls.
5. No band-aids will correct the unfair CPP/QPP discrimination, since it arises primarily from their earnings-related benefit formula and is exacerbated by the initial low percentage level adopted for contributions; rather, correcting the unfair CPP/QPP discrimination will require major surgery.

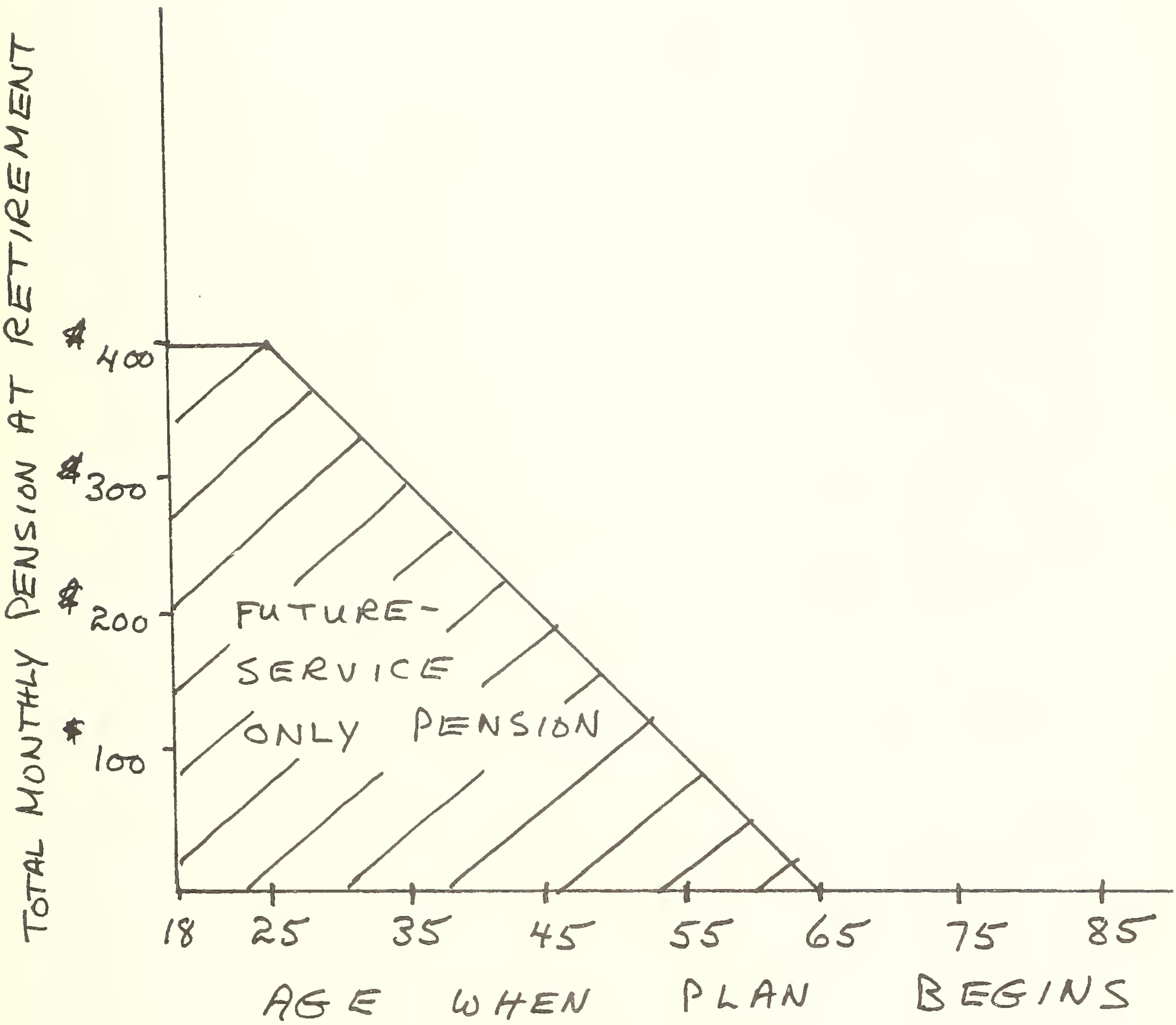
2
THE CPP/QPP AND PAST SERVICE

Regarding pension benefits for past service, the CPP/QPP retirement pensions differ fundamentally from the retirement pensions commonly negotiated by trade unions.

Negotiated flat benefits

Consider a typical negotiated flat benefit pension plan, paying a monthly retirement pension of $10 a month per year of service (say), with up to 40 years of service to count.

If only future service were counted for benefits, we would have the following:



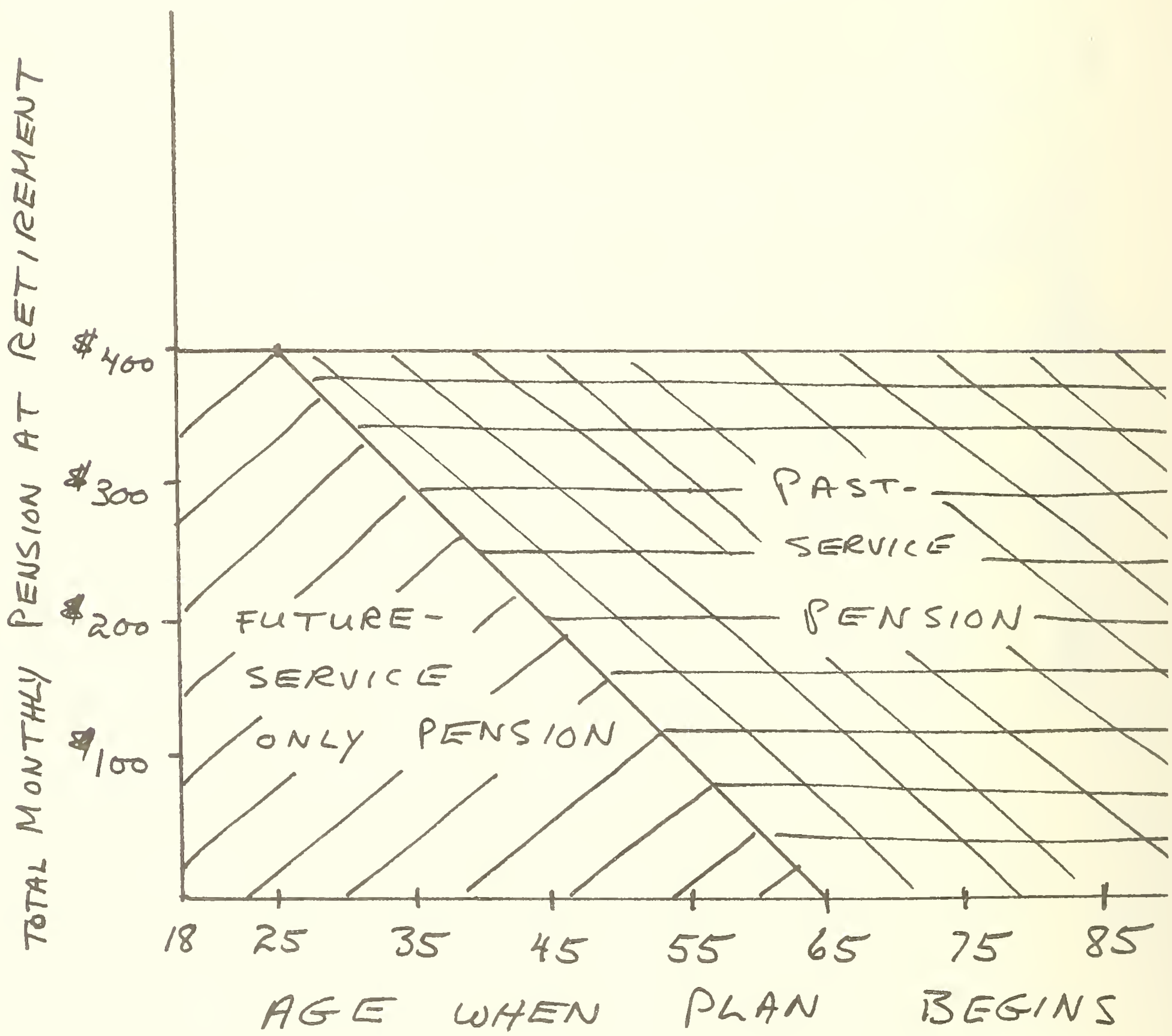
TOTAL MONTHLY PENSION AT RETIREMENT
$400
$300
$200
$100
FUTURE-
SERVICE
ONLY PENSION
18
25
35
45
55
65
75
85
AGE WHEN PLAN BEGINS

For someone aged 64 when the negotiated flat benefit pension plan begins, the future-service only benefit is derived thus:

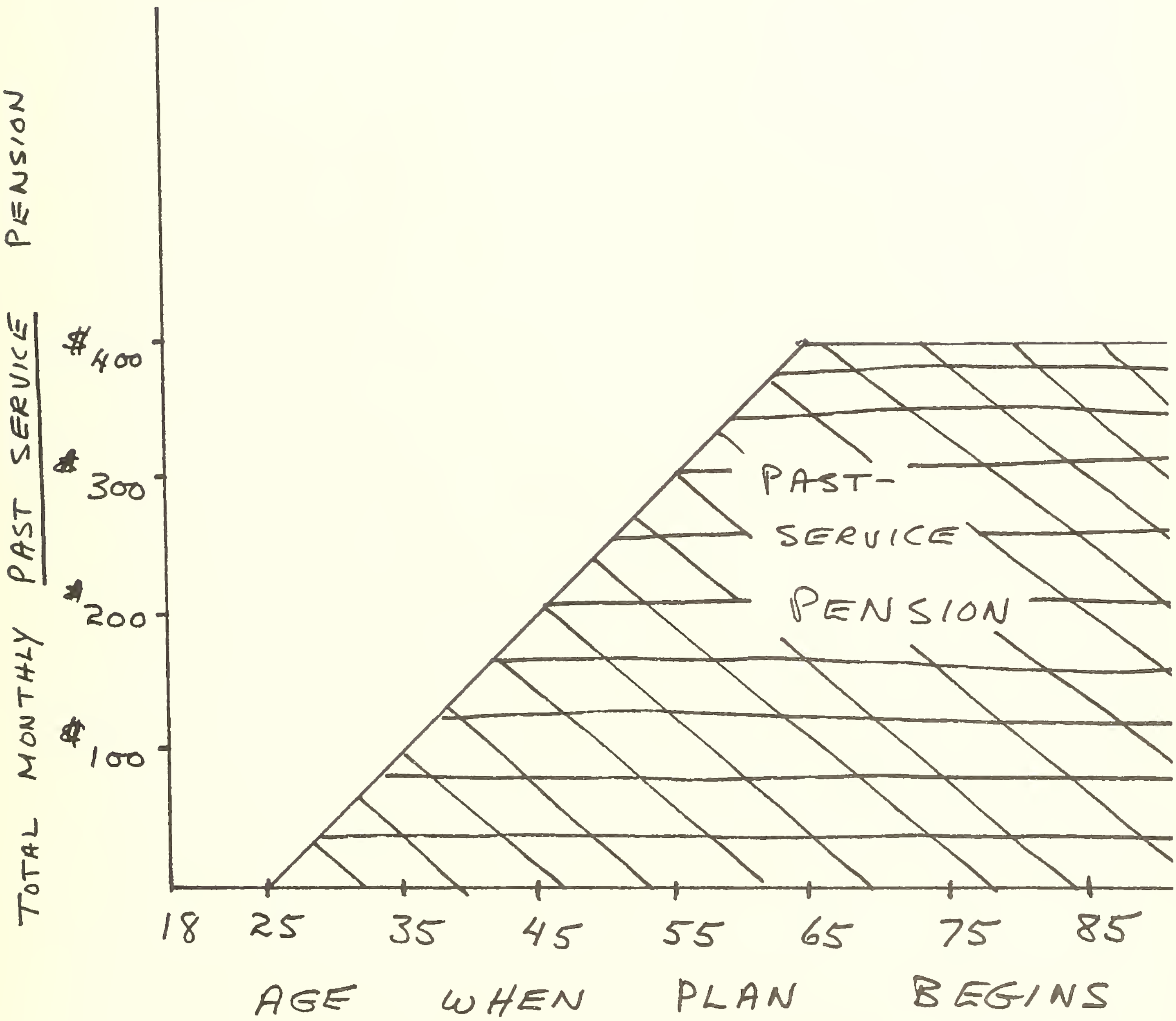
- future service = 1 year
- total service = 1 year
- monthly pension = 1 x $10

  = $10/month

To avoid such token pensions, commonly any employee covered when the plan begins will be given <u>full</u> past service credit, for <u>all</u> years of service (up to 40 years in total, in this example), as indicated below:



Now break out the past service pension benefits by themselves alone, and consider the profile they present, as follows:



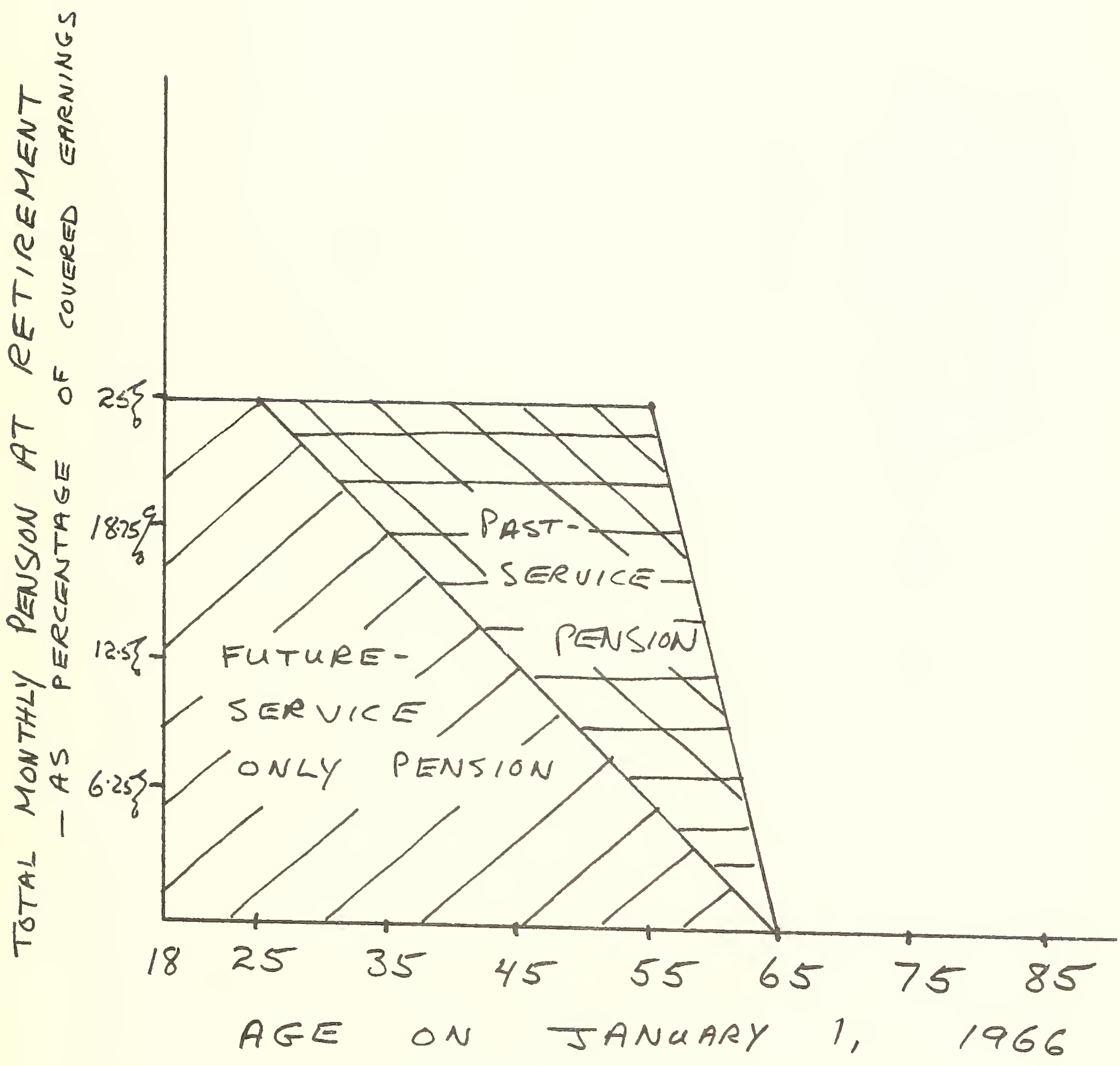
Note, for this negotiated flat benefit pension plan:

1. Maximum past service pensions are payable to all who are age 65 or over when the plan begins.
2. In a logical and orderly fashion, as age when the plan began diminishes, so the past service benefit granted to the individual dwindles accordingly, and the past service benefit is zero for all aged 25 or younger.

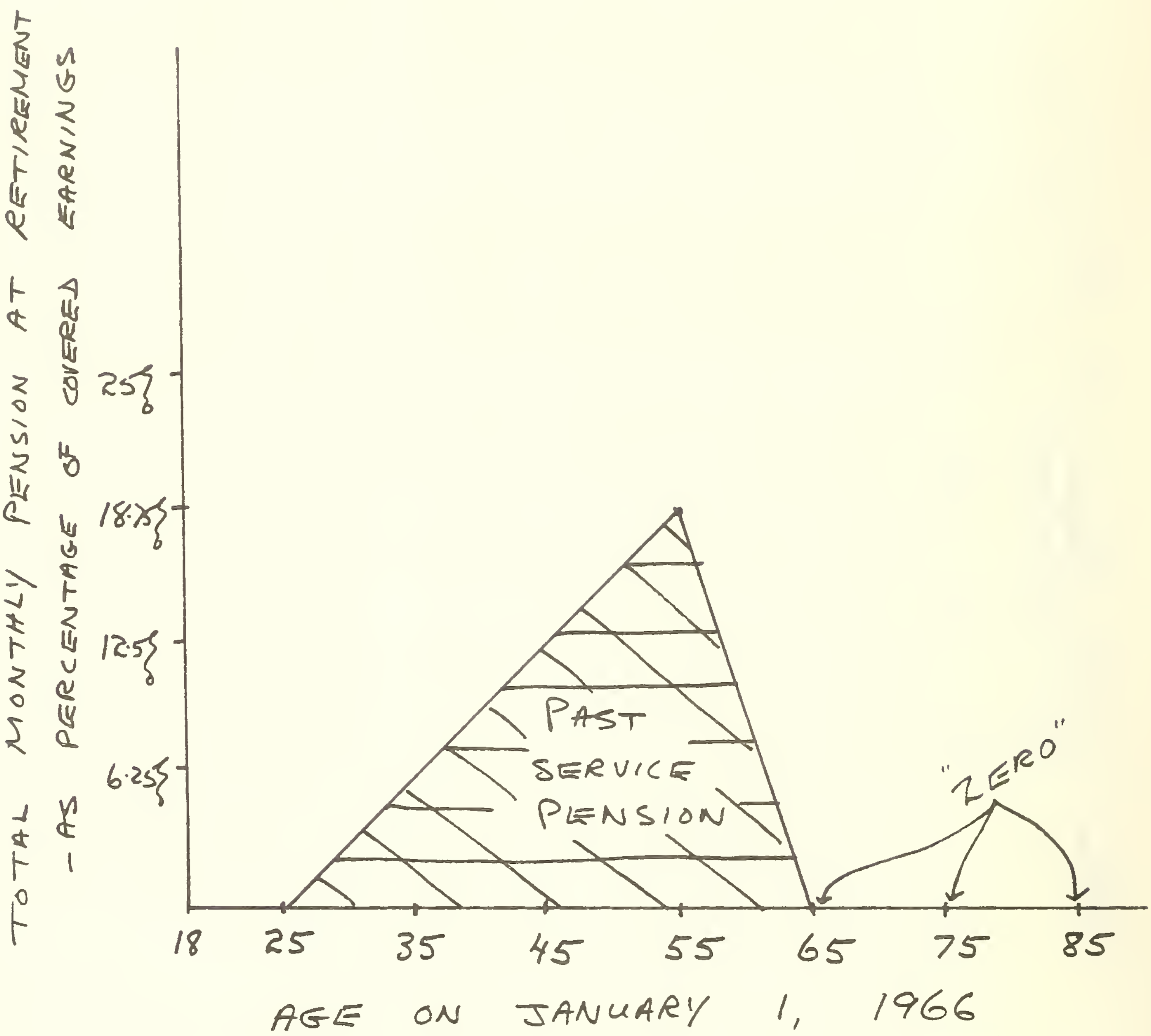
CPP/QPP

Now consider the CPP/QPP, and the comparable charts of benefits.

Assuming continuous full employment followed by retirement at age 65, for those at the ages shown when the CPP/QPP began (January 1, 1966), the profile has been:


TOTAL MONTHLY PENSION AT RETIREMENT
— AS PERCENTAGE OF COVERED EARNINGS
25%
18.75%
12.5%
6.25%
PAST-SERVICE PENSION
FUTURE-SERVICE ONLY PENSION
18 25 35 45 55 65 75 85
AGE ON JANUARY 1, 1966

Now, breaking out the CPP/QPP's past service component by itself, we have:



Note, for the CPP/QPP:

1. Maximum past service pensions were payable just to those who happened to be exactly age 55 when the CPP/QPP began.
2. In a logical and orderly fashion, as age when the CPP/QPP began diminished, so the past service benefit granted to the individual dwindled accordingly, and the past service benefit was zero for all aged 25 or younger.
3. However, as age went up above age 55, the CPP/QPP past service benefit rapidly decreased, and reached zero for all those aged 65 and up on January 1, 1966.

It is this last point - #3 - where the CPP/QPP past service benefits differ so fundamentally from the past service benefits of typical negotiated flat benefit pension plans. For age 65 retirements, the CPP/QPP gave progressively reduced past service benefits to those born between 1910 and 1901, with zero past service benefits to those born in 1900 or earlier. This is 'age discrimination' with a vengeance.

Apparently, in some form or another, the CLC's proposed doubling of the CPP/QPP retirement pensions from 25 per cent to 50 per cent would also incorporate no less a degree of punishing 'age discrimination'.

Government pensions - in general

For brevity, the above discussion concentrates on the CPP/QPP as they now exist. That is, Chapters 1 and 2 focus on those government pensions which happen to have 'upside-down generosity'. Of course, other specific design approaches are available for government pensions, and what follows below touches on these.

The key distinguishing characteristic is the nature of the subsidisation, that is which people benefit from the not-paid-for windfalls. There are three major varies:

1. Upside-down welfare: Larger not-paid-for subsidies/windfalls per month go to the fortunate higher income of the right age, with lower income people of the same age receiving smaller subsidies/windfalls per month. This is true of the CPP/QPP. It is also true in other countries, wherever government pension benefits are earnings-related, including under U.S. Social Security. Surely, given the facts, all major Canadian political parties - whether federal or provin-

cial - would not pick 'upside-down welfare' as their first choice for expansion of government pensions?

2. Neutrality - zero subsidies: Subsidies/windfalls under government pensions could be zero. That is, neither the higher-income people nor the lower-income people would be given something for nothing. Rather, benefits would be strictly contribution-related. This would be the case, for example, if government pensions were designed as mandatory RPA's (with separate male mortality and female mortality tables). Such mandatory RPA's, if so decided, could be invested by the private sector and could be integrated with existing employment pension plans. (See Chapter 11.) Provided government decision-makers are first satisfied that additional mandatory pensions are really required, to serve an income replacement role, then such zero-subsidy contribution-related pensions should appeal to all major political parties.
3. Right-side-up welfare: Larger subsidies/windfalls per month go to lower-income people, (and, in practice to women, and to higher-age pensioners). This is true of OAS, the GIS, and GAINS. Thus, benefits are people-related. Subject to an appropriate balance being struck between (a) working Canadians and taxpayers generally, vs. (b) Senior Canadians - all major Cnadian political parties appear likely to continue supporting substantial total amounts of people-related pensions.

Thus, in summary, regarding government pensions:

1. earnings-related benefits are politically unsuitable;
2. contribution-related benefits make sense (if, indeed, mandatory supplemental income replacement is found to be really necessary); and
3. people-related benefits - up to appropriate limits - are certainly required.

2
SUMMARY

1. Regarding past service benefits, CPP/QPP age retirement pensions differ fundamentally from the retirement pensions commonly negotiated by trade unions.
2. CPP/QPP past service benefits practice 'age discrimination' with a vengeance.

Canadians fancy that the taxation of income is levied at 'progressive' rates of taxation: for Senior Canadians, the facts are otherwise.

50 Per cent taxation

The Federal Guaranteed Income Supplement (the GIS), generally speaking, imposes 'taxation' on the incomes of lower-income Senior Canadians at a rate of 50 per cent. If you are a Senior Canadian and you are receiving a GIS payment, and you earn an additional $4 a month of income, then the GIS payments to you are normally reduced by $2 a month.

When you earn $4, and you lose $2 just because you earned the $4, then you are 'taxed' 50 per cent.

Thus, generally speaking, the GIS levies implicit taxation at a rate of 50 per cent.

100 Per cent taxation

Now consider a resident in Ontario who qualifies for both the GIS and also for GAINS payments. (GAINS stands for: Guaranteed Annual Income System).

Now suppose you earn an additional $4 a month. Then generally speaking, as a result, not only will your GIS monthly payment be reduced by $2, but also your GAINS payment will be reduced an additional $2.

You gain $4, but you lose an initial $2 and you also lose the second $2. Your net gain is zero.

Thus, in general, the GIS and GAINS in combination constitute 100 per cent taxation of income of those Senior Canadians covered by them both.

This highly 'regressive' general pattern of taxation is also generally in effect under the combined impact of the GIS plus the counterpart Provincial supplements payable to Senior Canadians in Alberta, British Columbia, Manitoba, and Saskatchewan.

Before examining some examples in more detail, first consider the two forms of taxation of income - explicit and implicit.

Explicit taxation of income

The regular taxation of income is administered by Revenue Canada and by the Quebec Ministry of Revenue. This regular system of income taxation is visible and obvious. In the technical jargon, it is called the 'explicit' system of taxation of income.

Under this explicit system of taxation, by and large those with the lowest incomes do indeed pay income tax at the lowest rates.

Those with the lowest incomes have the lowest marginal rates of explicit income tax, popularly called 'the lowest tax brackets'.

They also have the lowest average rates of explicit income tax, when their total explicit income taxes are averaged across their total incomes.

As incomes become larger, in general, the marginal rates become larger, and also the average rates become larger. This is a 'progressive' pattern of explicit income tax rates.

Implicit taxation of income

As well as the explicit taxation of income under the regular income tax system, there is also a considerable amount of 'implicit' taxation of the incomes of Senior Canadians.

Much or all of this implicit taxation is carried out at regressive rates of income tax. The lowest incomes of Senior Canadians are subject to some of the highest rates of taxation.

As already noted above, more than a few Senior Canadians are subject to implicit taxation at marginal rates of no less than 100 per cent.

25 Per cent taxation

Think of someone - anyone, whether a Senior Canadian or not - who has $800 a month to spend. That is, this person has $800 a month net, after

all taxation and all other statutory deductions.

Suppose this person works overtime and earns an additional amount of gross pay of $100. Suppose, further, that the net amount the person can spend only goes up from $800 to $875.

Then it is apparent that this person has earned an additional $100 but only has an extra $75 to spend. In other words, the additional income has been 'taxed' at the rate of 25 per cent.

In general, someone's income is taxed at 25 per cent when his extra spending is only three-quarters of his extra earnings - i.e. from his extra earnings he loses one-quarter, or 25 per cent.

The 25 per cent may be collected by Revenue Canada - i.e., explicit taxation of his income.

Or, the 25 per cent may be lost from his extra spending - not via Revenue Canada - but via 'a reduction in income security benefits'. For example, the person above may have been living in public housing, and when his income went up by $100 there could have been a $25 increase in his public housing rent. It all comes to the same thing. He only has $75 more to spend. He is 'taxed' 25 per cent.

This kind of taxation of income - via a reduction in social security benefits - is called implicit taxation.

To the person being taxed, to the person who earns another $100 but who only has an extra $75 to spend, it is exactly the same end result. It does not matter to him whether it be done via explicit taxation or via implicit taxation.

Thus, implicit taxation of incomes is an income tax.

Marginal rates of taxation

As indicated in Tables 1 and 2, the resultant marginal rates for 'taxing' the incomes of Senior Canadians are not progressive.

Rather, the marginal rates of 'taxation' of incomes of Senior Canadians are regressive. Those with the lowest incomes pay the highest marginal rates of taxation.

The details underlying Tables 1 and 2 are set out in Appendix B.

TABLE 1

MARGINAL RATES OF TAXATION

SENIOR CANADIANS - TWO TYPICAL SINGLE PERSONS*

'Other' income bracket (i.e. excluding OAS)		Marginal rate of taxation	
		Nova Scotia	Ontario
up to $ 1,174		50.00%	100.00%
$1,175 - 6,154		50.00%	100.00%
6,155 - 7,156		Nil	Nil
7,157 - 7,348	$113.00+	25.04%	73.70%
7,349 - 7,526		25.04%	23.68%
7,527 - 9,884		26.61%	25.16%
9,885 - 12,242		28.17%	26.64%
12,243 - 16,958		29.73%	28.12%
16,959 - 21,674		31.30%	29.60%
21,675 - 26,390		35.99%	34.04%
26,391 - 38,180		39.12%	37.00%
38,181 - 61,760		46.95%	44.40%
61,761 and up		53.21%	50.32%

* For details underlying the above Table 1, see Appendix B.

TABLE 2

MARGINAL RATES OF TAXATION

SENIOR CANADIANS - TWO TYPICAL MARRIED COUPLES*

'Other' income bracket (i.e. excluding OAS)	Marginal rate of taxation Nova Scotia	Ontario
up to $ 3,844	50.00%	50.00%
$ 3,845 - 9,488	50.00%	50.00%
9,489 - 10,224	Nil	Nil
10,225 - 10,416	$113.00+ 25.04%	73.70%
10,417 - 10,594	25.04%	23.68%
10,595 - 12,952	26.61%	25.16%
12,953 - 15,310	28.17%	26.64%
15,311 - 20,026	29.73%	28.12%
20,027 - 24,742	31.30%	29.60%
24,743 - 29,458	35.99%	34.04%
29,459 - 41,248	39.12%	37.00%
41,249 - 64,828	46.95%	44.40%
64,829 and up	53.21%	50.32%

* For details underlying the above Table 2, see Appendix B.

Average Rates of Taxation

Not surprisingly, since the marginal rates of the taxation of the Senior Canadian married couple illustrated in Tables 1 and 2 are regressive, so likewise the average rates of taxation applicable to the same Senior Canadians are likewise regressive. Those with the lowest incomes pay the highest average rates of taxation.

The resultant average rates of taxation applicable to the same Senior Canadians are illustrated in Tables 3, 4, 5 and 6.

The details underlying Tables 3, 4, 5 and 6 are set out in Appendix B.

TABLE 3

AVERAGE RATES OF TAXATION

SENIOR CANADIANS - TYPICAL SINGLE PERSON - NOVA SCOTIA*

"Other" income (1)	$'s of Taxation: GIS (2)	$'s of Taxation: Income tax (3)	Total $'s of Taxation = (2) + (3) (4)	Average Rate of Taxation (5)
Nil	Nil	Nil	Nil	Zero
$ 1,174	$ 587	Nil	$ 587	50.00%
6,154	3,077	Nil	3,077	50.00%
7,156	3,077	Nil	3,077	43.00%
7,157	3,077	$ 113	3,190	44.57%
7,348	3,077	161	3,238	44.07%
7,526	3,077	205	3,282	43.61%
9,884	3,077	832	3,909	39.55%
12,242	3,077	1,497	4,574	37.36%
16,958	3,077	2,900	5,977	35.25%
21,674	3,077	4,376	7,453	34.39%
26,390	3,077	6,073	9,150	34.67%
38,180	3,077	10,685	13,762	36.05%
61,760	3,077	21,757	24,834	40.21%

* For details underlying Table 3, see Appendix B.

TABLE 4

AVERAGE RATES OF TAXATION

SENIOR CANADIANS - TYPICAL SINGLE PERSON - ONTARIO*

"Other" income	$'s of Taxation			Total $'s of Taxation =	Average Rate of Taxation
	GAINS	GIS	Income tax	(2) + (3)+ (4)	
(1)	(2)	(3)	(4)	(5)	(6)
$ 1,174	$587	$ 587	Nil	$ 1,174	100.00%
6,154	587	3,077	Nil	3,664	59.54%
7,156	587	3,077	Nil	3,664	51.20%
7,157	587	3,077	$ 1	3,665	51.21%
7,348	587	3,077	141	3,805	51.78%
7,526	587	3,077	183	3,847	51.12%
9,884	587	3,077	776	4,440	44.92%
12,242	587	3,077	1,405	5,069	41.41%
16,958	587	3,077	2,731	6,395	37.71%
21,674	587	3,077	4,128	7,792	35.95%
26,390	587	3,077	5,732	9,396	35.60%
38,180	587	3,077	10,094	13,758	36.04%
61,760	587	3,077	20,564	24,228	39.23%

* For details underlying Table 4, see Appendix B.

TABLE 5

AVERAGE RATES OF TAXATION

SENIOR CANADIANS - TYPICAL MARRIED COUPLE - NOVA SCOTIA*

"Other" income	$'s of Taxation		Total $'s of Taxation = (2) + (3)	Average Rate of Taxation
	GIS	Income tax		
(1)	(2)	(3)	(4)	(5)
Nil	Nil	Nil	Nil	Zero
$ 3,844	$1,922	Nil	$ 1,922	50.00%
9,488	4,744	Nil	4,744	50.00%
10,224	4,744	Nil	4,744	46.40%
10,225	4,744	$ 113	4,857	47.50%
10,416	4,744	161	4,905	47.09%
10,594	4,744	205	4,949	46.72%
12,952	4,744	832	5,576	43.05%
15,310	4,744	1,497	6,241	40.76%
20,026	4,744	2,900	7,644	38.17%
24,742	4,744	4,376	9,120	36.86%
29,458	4,744	6,073	10,817	36.72%
41,248	4,744	10,685	15,429	37.41%
64,828	4,744	21,757	26,501	40.88%

* For details underlying Table 5, see Appendix B.

TABLE 6

AVERAGE RATES OF TAXATION

SENIOR CANADIANS - TYPICAL MARRIED COUPLE - ONTARIO*

"Other" income (1)	$'s of Taxation GAINS (2)	GIS (3)	Income tax (4)	Total $'s of Taxation = (2) + (3)+ (4) (5)	Average Rate of Taxation (6)
$ 3,844	$1,922	$1,922	Nil	$ 3,844	100.00%
9,488	1,922	4,744	Nil	6,666	70.26%
10,224	1,922	4,744	Nil	6,666	65.20%
10,225	1,922	4,744	$ 1	6,667	65.20%
10,416	1,922	4,744	141	6,807	65.35%
10,594	1,922	4,744	183	6,849	64.65%
12,952	1,922	4,744	776	7,442	57.46%
15,310	1,922	4,744	1,405	8,071	52.72%
20,026	1,922	4,744	2,731	9,397	46.92%
24,742	1,922	4,744	4,128	10,794	43.63%
29,458	1,922	4,744	5,732	12,398	42.09%
41,248	1,922	4,744	10,094	16,760	40.63%
64,828	1,922	4,744	20,564	27,230	42.00%

* For details underlying Table 6, see Appendix B.

OAS to be Income Tested?

Suppose now OAS were to be income tested, i.e, suppose OAS were to be rolled into the GIS and thus be subject to a 50 per cent rate of hidden taxation.

If that were done, the average rates of taxation on 'other' income would be further increased on all incomes where there is no GIS eligibility. In 1983, this would mean that average rates of taxation for single Senior Canadian would be higher than shown in Tables 3 and 4 for all 'other' incomes equal to $6,155 or over. For Senior Canadian married couples, the average rates of taxation would be higher than shown in Tables 5 and 6 for all 'other' incomes equal to $9,489 or over.

Already those average rates of taxation are excessively high. They should not be yet further inflated by the single, isolated change of merely income testing OAS.

Hence, it would be a major step in the wrong direction just to make the one change of income testing OAS.

Comparison of Rates of Taxation

Compare (a) the marginal rates of taxation applicable to a working Canadian aged 64 or younger, with (b) the marginal rates of taxation applicable to the 'other' income of a Senior Canadian.

Over the first bands of income, which are relevant to most working Canadians, the total marginal rate of taxation is appreciably below 50 per cent, and commonly below 35 per cent/30 per cent. This is so even aggregating all elements of taxation of income, e.g.:

- federal income tax
- federal Child Tax Credit tax-back
- provincial income tax
- UIC premiums
- CPP contributions
- etc.

In retirement, on the other hand, 'other' income is - more often than not - taxed at least 50 per cent and possibly even 100 per cent.

Is it any wonder that RRSP's are less and less popular amongst working Canadians with lower and lower incomes, and that Senior Canadians 'shift assets' to younger relatives to minimise the impact of the 50 per cent/100 per cent implicit taxation of the GIS/GAINS?

3

SUMMARY

1. The incomes of the majority of Senior Canadians are taxed at least 50 per cent both on a marginal basis and on an average basis.
2. More than a few Senior Canadians have their incomes taxed 100 per cent.
3. In general, the Senior Canadians with the lowest incomes are in the highest tax brackets.
4. This unfair taxation of Senior Canadians removes much of the incentive before age 65 to save for retirement - rather, for working Canadians there is every incentive to spend/spend/spend, so as to maximize GIS/GAINS payments.
5. No band-aids will easily correct the unfair taxation of Senior Canadians, since it impacts so heavily on so many of them; rather, correcting the unfair taxation of Senior Canadians will require <u>major surgery</u>.

4

OTHER AVENUES TO SEARCH - OTHER STONES TO TURN

Chapter 2 shows that what we may fancy to be the pattern of subsidies to Senior Canadians by income level, is not in fact always the case.

Chapter 3 shows that what we may fancy to be the pattern of taxation of the incomes of Senior Canadians is not in fact the case.

Those differences between our fancies and the facts should be given serious consideration. Now and the immediate future would be a good time to tackle these issues, in conjunction with the National Pension Debate.

No significant decision should be made in the National Pension Debate, until ample efforts have been made to adequately analyse and debate these central subjects of taxation and subsidy.

Only by adopting an appropriate and central framework as to taxation and subsidy will it then be possible to build a durable and desirable system for Senior Canadians.

By way of setting out an initial agenda for such detailed consideration, some issues related to these central concepts of taxation and subsidy are touched on below.

Levels of Taxation

If the individual knows or senses that he or she will be more heavily taxed in retirement than while working, how does this affect incentives to work and to save?

In retirement, the level of taxation on low levels of income is at least 50 per cent, both as a marginal rate and as an average rate. Often it is higher, in fact ranging up to 100 per cent.

What are the detailed by-products of such comparatively high rates being levied against Senior Canadians with the lowest incomes?

Fluctuations in Income

Speaking generally, the income of a Senior Canadian receiving a Guaranteed Income Supplement (GIS) payment is 'tested' only once a year.

The same applies to recipients of benefits under the counterpart Provincial supplement programs in effect in the Provinces of Alberta, British Columbia, Manitoba, Ontario and Saskatchewan.

Where a Senior Canadian does not have a level income - i.e. does not have a literally 'fixed' income - then he or she may endure hardship. This is because the fluctuations in his income are only roughly adjusted to by the levels of GIS payments, on account of the income-test happening only once a year.

An Illustration

This may be illustrated in Table 7.

In this illustration, it is assumed that the Senior Canadian is married, is living in Ontario, is retired, and has no other income retirement income except a monthly CPP pension of $100 a month.

For simplicity, it is assumed that there is no inflation. (Of course, since there actually is inflation, all the figures become escalated upwards, but the same general basic pattern holds good.)

TABLE 7

FLUCTUATIONS IN MONTHLY INCOME

Time period (1)	Total monthly Government pensions (including CPP) (2)	Monthly income from Working (3)	Total monthly income = (2) + (3) (4)
Jan. 1984 to Dec. 1984	$1,092.12	Nil	$1,092.12
Jan. 1985 to Mar. 1986	$1,092.12	$200.00	$1,292.12
Apr. 1986 to Dec. 1988	$ 892.12	$200.000	$1,092.12
Jan. 1989 to Mar. 1990	$ 892.12	Nil	$ 892.12
Apr. 1990 onwards	$1,092.12	Nil	$1,092.12

This married couple would be eligible to receive total income as shown in the attached table, amounting to an estimated $1,092.12 a month from January 1984 onwards.

Extra Earnings Begin

Now suppose that the husband takes a part-time job, and earns another $200 a month, from January 1985 onwards.

Those additional earnings are not taken into account in the 1985 income test that considers the calendar year 1984. Hence, they are not taken into account by the GIS income test until the end of March 1986. A reduction is only made in GIS payments, and in the counterpart Ontario supplement payments (the GAINS payments), effective April 1986.

As of April 1986, the $1,092.12 a month is reduced by $200.00 a month, down to a new level of $892.12 a month.

Extra Earnings End

Now suppose that the additional earnings from working, of $200.00 a month, cease at the end of December 1988. Then, in the normal way, the drop in income will not result in larger GIS and GAINS payments until that first payable in April 1990.

From January 1989, all the way to March 1990, the government pension total will remain at merely $892.12.

Only on April 1990, will the government pension total go back up to $1,092.12.

Difficult to Budget

The final column in Table 7, column (4), shows that the spendable income of this Senior Canadian couple rises, and then later falls, in a way which makes it difficult for them to budget their living costs.

It goes from $1,092.12 up to $1,292.12; returns to $1,092.12 sinks to $892.12; and then returns to $1,092.12.

There are special provisions whereby Senior Canadians may make specific application to have such fluctuations in income ironed out. But how many Senior Canadians know that such special provisions are available?

Further, how many Senior Canadians know that, as in this particular example, the entire amount of additional income will be 'taxed away'? If they did know, would they decide not to make the effort, thereby not only losing the income but also failing to benefit the national economy and likewise failing to give themselves the other inherent benefits that come from doing work for pay?

Public Housing

There is much discussion of the possibility of building additional housing for Senior Canadians.

However, how much have the advocates of public housing for Senior Canadians talked with Senior Canadians themselves about some of the detailed impacts?

An Example

For example, consider two Senior Canadians with closely similar incomes. See what happens when one has just too much other income (possibly from an RRSP or from savings) to qualify for public housing, but the other one has a just low enough income to qualify. The first is denied public housing, while the second is admitted.

Because of the significant subsidies built into public housing for Senior Canadians, the second person gains considerably. In fact, although that second person may have worked less and have saved less, and hence has a lower starting income in retirement, he may well have more spendable income thanks to the significant public housing subsidy.

Is this fair?

Adequate Income the Key

In any event, is the problem really a housing problem, or an income problem?

If the problem is really one of income, should it not preferably be addressed in terms of the taxation-subsidy system, and not via public housing?

After all, we do not (or not, at least, as yet) provide 'public clothing' or 'public food' to Senior Canadians. Rather, we leave it to their

good judgement to spend the income at their disposition. Individual tastes vary.

Surely, the great majority of Senior Canadians have the wit and widsom to decide how best to make their own expenditures, including their housing expenditures, if only they have adequate incomes?

Surely, therefore, we should look again, and very carefully, at public housing?

Perhaps all subsidies should be removed from public housing, with those subsidy monies then more fairly and more efficiently paid out to Senior Canadians via suitably increased income security payments?

The CPP and the Working Poor

Consider the working poor in a province having a counterpart Provincial supplement program, such as Ontario for example.

In Retirement

Since we are considering the working poor, let us suppose that these people arrive at normal retirement with no RRSP or other personal savings for retirement, and with no employment pension plan entitlement. Thus, suppose that their monthly retirement income comes exclusively from Government sources, i.e. OAS, the GIS, the Ontario GAINS payments, and the CPP.

The CPP payments are 'taxed 100 per cent' - i.e. taxed 50 per cent by the GIS reductions and then also taxed again a second 50 per cent by the GAINS reductions. Thus, in retirement, those people have the same income to spend, whether they receive the CPP retirement pension, or not. Their CPP contributions achieve nothing for their retirement.

Thus, Ontario working poor persons reaching retirement will be no further ahead by reason of having contributed to the CPP.

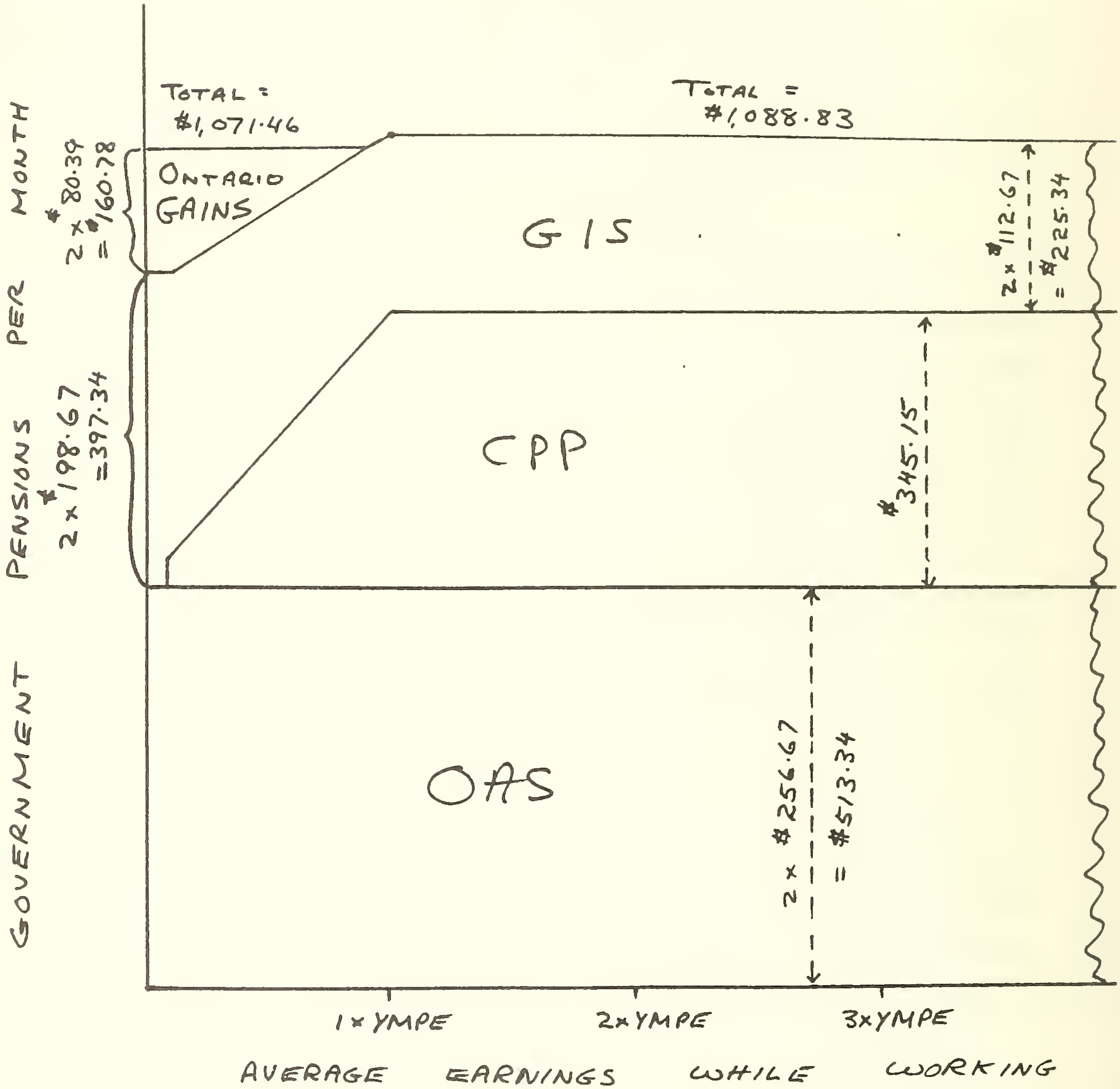
Chart 2, illustrates the picture for a married couple with no private sectore retirement income. Then, even with zero CPP, monthly income still totals $1,071.46 in the third quarter of 1983. This is level and unchanged, until the monthly CPP benefit goes well above $300 a month - a figure which will not be attained by the working poor.

CHART 2

SAMPLE 'SCHEMATIC' ILLUSTRATION

FLAT BENEFIT OVERALL

- married couple, both on OAS
- residents of Ontario
- no private sector retirement income
- one spouse in paid employment before 65
- July-August-September, 1983



Prior to Retirement

The existence of the CPP, however, does make a difference prior to retirement.

Here, the CPP imposes a contribution on the working poor while they are working, without in any way later on improving their retirement income. (Remember, this still refers to Ontario and the other Provinces having counterpart Provincial supplement programs.)

Does it make sense that, in these five Provinces, the working poor - of all Canadians - should be required to pay into the CPP while they are working, yet receive no additional income to spend in retirement as a result?

Administrative Overheads

Do all these complexities raise Government administrative overheads, and if so by how much?

Taxation

For example, is it really necessary that the incomes of Senior Canadians in Ontario be 'taxed' not only by Revenue Canada, but also by the Federal Department of National Health and Welfare (via the GIS income-test), by public housing authorities (via rents that are income-related on a sliding scale), and by every other existing measure (or proposed measure) of income-testing and 'selectivity'?

Would it not be more economical to have all income-testing simply carried out by a single taxation body, namely Revenue Canada?

Subsidies

As another example, the CPP is actually a 'flat' benefit, i.e. of equal amount, for all Senior Canadians born in the same year and who have been continuously employed since the beginning of 1966 at earnings at least equal, year-by-year, to the CPP YMPE (Year's Maximum Pensionable Earnings).

All that happens is that the CPP pays less and less to those who earned less and less than the YMPE.

However, the CPP is not alone. There is also the GIS. Again, there are also the counterpart Provincial supplement programs. See again Chart 2. This shows that for an Ontario married couple the tapering off of the CPP for those with lower incomes is largely cancelled out by the GIS plus GAINS.

To a large extent, 'what the CPP taketh away, the GIS plus GAINS giveth back'.

So what is achieved by all these ramifications?

Why not combine everything into a single flat benefit payment - be done with it - and reap administrative savings?

Gap in Take-Up

Another major problem is the gap in the 'take-up' of the GIS. That is, many eligible for the GIS do not apply for it, and hence do not receive it. The following is reprinted with the permission of Mr. Robin Schiele, Editor, 'Benefits Canada', from the November/December 1982 issue:

'There are 184,000 senior Canadians who are not being paid monthly cash that rightly belongs to them.

'Yes, every month, Health and Welfare Canada is not paying out an estimated 184,000 monthly Guaranteed Income Supplement (GIS) and Spouse's Allowance payments for which senior Canadians are eligible if only they would apply.

'One of those estimated 184,000 may be your aunt/uncle, your mother/father, or a former employee. You might, therefore, like to know how much monthly income such a person is allowed to have, including Old Age Security (OAS) and still be eligible for at least a partial GIS benefit.

'A married couple, both of whom are receiving OAS, is eligible for the GIS if their monthly income if $1,261.83 or less. This monthly income comprises the two OAS cheques of $246.92 each and a further $767.99. That's an annualized income of $15,141.96.

'The accompanying table sets out the full picture for the final calendar quarter of 1982.

How much you can earn and still claim GIS

	OAS	Other Allowable Income	Maximum Allowable Monthly Income	Maximum Allowable Annualized Income
Single, including widowed and divorced, receiving OAS	$246.92	$ 495.99	$ 742.91	$ 8,914.92
Married (both receiving OAS)	493.84	767.99	1,261.83	15,141.96
Married (one receiving OAS, the other aged 60-64)	246.92	1,343.16	1,590.08	19,080.96
Married (one receiving OAS, the other under 60)	246.92	1,238.91	1,485.83	17,829.96

'Now, why does Health and Welfare Canada tell us that, to qualify for GIS, someone must have 'little or no other income'? (See, as one example, Canadian Governmental Report on Aging, June, 1982).

'Does the average person in the street consider those maximum monthly income levels in the table to be really so 'little'? In future, why not encourage the missing 184,000 to apply by telling them the qualifying incomes for GIS eligibility in dollar amounts, as in the accompanying table?

Cat food

'The next time you hear about a senior citizen having so little cash that he/she is forced to eat 'cat food', have a glance at the person's monthly income. Is the person in fact, eligible for the GIS but the GIS isn't being paid?

'Perhaps there would be less poverty amongst senior Canadians is those missing 184,000 GIS benefits were actually paid every month?

The GIS not 'welfare'

'If a senior Canadian drags his feet in applying for the GIS because he has heard it is akin to 'welfare,' tell him it isn't so.

'The GIS is not 'welare' in the usual sense of the word. Rather, the GIS is income security and is clearly related to OAS, thus:

'1. The GIS is free from welfare-type 'asset testing.' Rather, the GIS does simple 'income testing.'
'2. The GIS is paid under the same, single Act of Parliament as OAS.
'3. Normally, the GIS and OAS are paid in the same, single monthly cheque.

'Because of all that, the GIS has none of the stigma of welfare.

'Worth the effort?

'If income is close to the maximum for GIS eligibility, is it worth the effort to apply when the person's partial GIS may only be a few cents a month? Sure, it most certainly is worth applying, and the sooner the better.

'You see, when the GIS goes up with inflation each calendar quarter, everyone is given the same dollars-and-cents monthly increase. Thus, for example, all GIS benefits to single senior Canadians - whether full GIS or partial - were $7.22 greater in October 1982 than they were in September 1982.

'So, at the extreme limit, even if the partial GIS benefit was only 67¢ a month in September, then that same benefit went up in October by $7.22 to become $7.89. And so on, and so on, into future calendar quarters.

'In a word - the sooner the better for each and every one of those missing 184,000.'

Note: The source of the above estimate, i.e. 184,000, is the article by Daly.

4

SUMMARY

1. The GIS, in actual practice, fails to respond appropriately to fluctuations in incomes of Senior Canadians. Their spendable incomes, therefore, tend to rise - and fall - in an erratic way which makes it difficult for them to budget.
2. As between two Senior Canadians with closely similar incomes, and with one lucky enough to be in public housing but the other not, the net results of the public housing subsidies are unfair.
3. In many cases, the CPP does <u>not</u> put the 'working poor' any further ahead in retirement - their CPP benefits are 100 per cent taxed-back by GIS/GAINS. On the other heand, <u>before</u> retirement, the CPP does make a difference to the working poor - <u>negatively</u> - since the CPP contributions <u>reduce</u> their spending power while working.
4. Needless complexities in government pensions raise Government administrative overheads.
5. An estimated 184,000 Senior Canadians are eligible to receive GIS benefits, but have not applied for them and are therefore not receiving them.
6. The above are all serious defects of existing government pensions. Band-aids are not the answer. Major surgery is.

5
LARGE COSTS

Just for the sake of argument, suppose for a moment that all of the foregoing major problems could be rectified with no 'losers' anywhere - just winners.

That would be hugely costly.

Upside-Down Windfalls

Suppose, for example, that the substantial upside-down windfalls paid monthly by the CPP/QPP to higher-income pensioners were all left intact, and that lower-income pensioners were 'levelled up' by paying them equally generous CPP/QPP monthly windfalls.

Clearly, that would entail additional CPP/QPP retirement pension expenditures of hundreds of millions of dollars annually.

Hidden Taxation

Suppose, as another example, that the maximum GIS benefit amounts were all left intact, and that the impact of the GIS 50 per cent tax-back rate were 'softened' by cutting this rate down to (say) 30 per cent.

Clearly, that would also entail additional government pension expenditures of some further hundreds of millions of dollars annually.

Working Canadians

Having only winners - and no losers - would have a substantial adverse impact on working Canadians.

There is, therefore, no easy way out, whereby every Senior Canadian can be a winner at a trifling cost to working Canadians. That is one option which just does not exist.

Another option, perhaps, would be to leave things pretty much as they are, with the addition of a few band-aids here and there. The trouble is, such a stand-pat option would mean perpetuating both:

(a) gross inequities in windfalls and subsidies, and

(b) gross inequities in the taxation of the incomes of Senior Canadians.

These inequities are just too gross to be tolerated by Canadians as a whole forever.

Sooner or later, real 'reform' must come.

But, certainly, real reform must be implemented at a total cost which is affordable to all concerned - especially working Canadians.

Consequently, the other option is the viable one, whereby inequities are rectified, with a tolerable mixture of winners and losers, and with costs to working Canadians kept affordable at all times. This will require major surgery.

5

SUMMARY

1. Banishing all inequities by spending more money - i.e. having only winners with no losers - is not a viable option. It would cost too much.
2. Leaving things as they are is not a viable option. The subsidy inequities and the taxation inequities are too far out of line to be tolerated forever.
3. Sooner or later, therefore, there must be both
   (a) real reform, plus
   (b) effective cost control.

   This will require major surgery, over a period of time.

Subsidies

We need to obtain better value from Government pension monies for Senior Canadians, so as to keep within a total cost budget yet satisfying the existing large areas of sharpest priority for those most in need.

Therefore, it is essential that the mechanics and the pattern of subsidies in Government pensions for Senior Canadians be in accord with commonsense.

As between <u>any</u> two Senior Canadians living side by side, anywhere - and where either both are single or both are married - the subsidy should be greater for the one with the lower income from private sources, and the subsidy should be less for the one with the higher income from private sources.

Surely the great majority of Canadians would agree that we should move as far and as fast towards that target as may be reasonably possible?

Taxation

Speaking generally, in practice, the private incomes of Senior Canadians are now taxed from <u>the first dollar</u> of such 'other' income, with no deductions and no exemptions.

They are at least taxed 50 per cent by the GIS, and they are sometimes taxed 100 per cent by the combined impact of the GIS reductions and the reductions of the counterpart Provincial supplement programs.

Since Old Age Security is universally payable, this taxation of 'other' income from <u>the first dollar</u> onwards is not only in order, it makes good taxation sense.

However, it is unfair that the rates of taxation - both the marginal rates of taxation and the average rates of taxation - are so high on those Senior Canadians with the lowest incomes, and even on many of those with moderate incomes.

Surely the taxation of incomes of Senior Canadians should be carried out at rates of taxation which are more moderate on the lowest incomes, and also at rates which are no longer regressive?

As a 'better buy', there could be a single level rate of taxation on a wide band of low and moderate incomes, from the first dollar onwards, at a more reasonable level than 50 per cent, let alone 100 per cent. Then there could be progressive increases later, on higher incomes, at the same average rates as in effect now.

The initial 'single level rate of taxation' could vary as required from Province to Province. This rate could be withheld at source, so that the great majority of Senior Canadians would no longer have to pay income tax instalments. At assessment time, those with charitable contributions would receive an appropriate refund.

Surely, this would be more in keeping with the general Canadian concepts of fairness in taxation?

Surely the more moderate rates of taxation on lower incomes and on moderate incomes, would also provide more realistic encouragement to working and saving?

Freedom

Surely the Government pensions and the taxation of incomes for Senior Canadians should not decrease their freedom, but should rather increase it?

Surely Senior Canadians should have the freedom to spend their incomes as they see fit, including their incomes ear-marked for housing?

Administration

Surely the arrangements should all be easy to understand and easy to deal with?

Certainly those liable to pay taxation on their incomes should indeed pay it.

But the other side of that coin, surely, is that where a Senior Canadian is entitled to receive any Government pension monies, then every reasonable effort should be made to see that the Senior Canadian actually receives such monies?

An estimated 184,000 Senior Canadians are not now receiving the partial GIS payments to which they are entitled by their income levels. The present mechanics in delivering those partial GIS payments entail costs that are larger than necessary - partly administrative overhead costs, but also not least costs in human terms for those making the applications.

Surely we should consider alternative mechanics that require less work within the Civil Service and which are significantly easier for the Senior Canadians themselves, and which will see that every last Senior Canadian eligible for the GIS actually receives it?

In a related sense, for those Senior Canadians with fluctuating incomes - for example on account of part-time work - surely the taxation and subsidy arrangements affecting them should be as responsive as possible to accommodate their fluctuating incomes?

Society as a Whole

Surely there is even more involved here than the well-being of Senior Canadians and the tax burdens on the rest of us who are not yet Senior Canadians?

Surely we all benefit when Senior Canadians are treated adequately, fairly, and with faith in their own judgement and in their sense of responsibility?

In a Word

We have allowed our system of taxation and subsidies for Senior Canadians to just grow up of its own accord, as it were. We should now look at alternatives.

In simply adding a bit here and then adding another bit there - as we tinkered with band-aids to our system - we have been focusing too much on technicalities. As a direct result, we have given rise to many undesirable by-products, in areas of taxation and subsidy, and, most importantly, by way of their results on people.

We have been putting the cart before the horse, i.e., we have been putting technicalities before results.

It is results that really count - results in terms of people and money. Why not, therefore, consider people and money first, and see what major surgery is required?

Mish-Mash Unnecessary

There is no real necessity for the income of a Senior Canadian to be subject to possible 'taxation' by so many possible administrative systems, including in Ontario for example:

- Revenue Canada
- National Health & Welfare (i.e. under the GIS)
- the Ontario Ministry of Revenue (i.e. under GAINS)
- public housing
- plus any other means-tested or income-tested program.

Similarly, when the aim is simply to 'subsidise those Senior Canadians who need subsidising', there is no real necessity to provide varying amounts of subsidies, sometimes in overlapping or conflicting directions, under so many possible programs, including in Ontario, for example:

- Old Age Security
- the Guaranteed Income Supplement
- GAINS
- Ontario Tax Grants
- the Canada Pension Plan
- public housing
- rebates on municipal taxes
- reductions in charges for public transportation
- etc., etc.?

If we were setting up a fresh system of taxation and subsidy, from scratch, would we really have this complex array of disparate and sometimes uncoordinated arrangements?

No. It is simply that all these measures have simply appeared and grown up, taking a life of their own. The sooner we take conscious charge of it all, and turn it into a 'better buy' for Canadian consumers, the better.

We sometimes fancy that the income tax system and the income security system are quite separate and distinct systems.

This could possibly be the case if Canadians were sharply divided at two extremes into the rich and into the poor.

The facts are, of course, that Canadians have incomes varying continuously across the possible spectrum. Moreover, Canadians - including Senior Canadians - do not all have constantly static levels of income. More than a few Senior Canadians have fluctuating levels of income.

For these commonsense reasons alone, in fact we need to consider jointly - at one and the same time - both the income tax system, and the income security system.

When we reconsider income tax for any group such as Senior Canadians - we should reconsider income security for Senior Canadians at the same time.

Likewise, whenever we reconsider income security for Senior Canadians - we should also simultaneously reconsider the income taxation of Senior Canadians.

Three of the first people to recognize this and to put matters on the records, did so in the United Kingdom, in the early 1940's. One was the Lady Juliet Rhys Williams and the two others were both U.K. actuaries, a Mr. A.T. Haynes, F.I.A., F.F.A., and a Mr. R.J. Kirton, M.A., F.I.A.

Their message that both income tax and income security should be given joint and simultaneous consideration has been echoed since, in a number of instances, including:

- the 1972 official U.K. Government Green Paper entitled, 'Proposals for a Tax-Credit System'
- the paper by the author of this present discussion, presented to the 1972 Annual Conference of the Canadian Tax Foundation entitled, 'Income Tax vs. Income Security'
- from time to time in the weekly U.K. publication 'The Economist'
- in the report of a U.K. Committee headed by Prof. J.E. Meade, published in the U.K. in 1978 and entitled, 'The Structure and Reform of Direct Taxation'

- increasingly in some quarters in our Canadian Federal and Provincial Governments; one encouraging example consists of the coordinated and simultaneous changes in Quebec, concerning Provincial Income Tax and Provincial Family Allowances.

Where to Begin

The underlying good sense of giving joint consideration to income security and income tax is becoming acknowledged more widely.

The next question is, where does one begin in overhauling what we now have in Canada for Senior Canadians?

One possibility would be to recognize that many Senior Canadians have virtually zero income from private sources. Of the 2,431,285 Senior Canadians receiving Old Age Security in July 1983, no less than 302,643 or 12 per cent of them, were receiving a maximum Guaranteed Income Supplement.

Consequently, it should be recognized that Old Age Security by itself is not the upper limit of subsidisation. Rather, the upper limit of subsidisation per person is at least Old Age Security plus the Guaranteed Income Supplement. The upper limit of subsidisation could be more or less higher than this, depending upon the existence in a Province of additional subsidisation via a counterpart Provincial supplement program (e.g. GAINS in Ontario), Provincial tax credits (e.g. Ontario Tax Credits), subsidies under public housing, etc.

Subsidies

The most logical, most efficient, and most sensible step would be to pay all Senior Canadian in any given Province the maximum monthly level of subsidisation, in a single monthly payment. The only variations in any one Province would be as needed in relation to housing (see Chapter 8).

Eventually, it would be possible to reduce the number of subsidisation payments to any given Senior Canadian to rock bottom minimum of one a month - i.e. twelve a year. A single application for Old Age Security would result in a single non-taxable monthly payment, depending only upon the Province of residence and upon the housing situation of the recipient (see Chapter 8).

Taxation

In taxing the 'other' income of Senior Canadians, there would then be no need for personal exemptions.

Taxation could begin on the first dollar of 'other' income, i.e. private income received from all other sources.

Such taxation could be progressive, with the initial tax bracket having a single rate (per Province) across a wide range of income.

Such single rate could be less than 50 per cent.

If income taxes were withheld at that single rate per Province, there would then be many Senior Canadians who would be subsidised and taxed without ever having to file an income tax return.

It would all be flexible, adapting at once to fluctuating incomes.

Yet it would also be precise - exact - easy for the individual - and economical to administer.

As first published in the May 16, 1983 issue of 'Canadian Business Management Developments', and reproduced with the permission of Mr. J.N. Grace, Managing Editor, CCH Canadian Limited, Don Mills, Ontario, M3C 1Z5:

'Intermingling

'In summary, (a) the income security system imposes hidden taxation, and, (b) the income tax system accords income security benefits. The two systems are intermingled.

'Actually, they are really part and parcel of one, single system - 'the tax-transfer system'. Looking at both income security and at income tax, at one and the same time, is the key to achieveing both better selectivity and reasonable incentives.

'Tax-Transfer System

'The key is to focus on the total, combined end results of the tax-transfer system as a whole, as it impacts on each individual Canadian.

'(a) How much is his gross income (if any) before all income taxes, and before all income security benefits?
'(b) How much is his net income after all income taxes, and after all income security benefits?
'(c) What is the net change between these two figures?

'It is that net change that counts.

Simple Example

'Consider a single Senior Canadian, living in New Brunswick, in the second quarter of 1983. Suppose that he has private income of exactly $400 a month.

'Then (A) at present, with the income security system kept separate from the income tax system, his income tax is nil, but his GIS payment is reduced by 50 per cent of his $400 monthly income, i.e., his GIS is reduced $200 a month.

'On the other hand, suppose we had a single, unified tax-transfer system in Canada. What follows is purely by way of an initial illustration as to the simplicity of the mechanics involved. Then (B) under such a unified tax-transfer system, income tax could be deducted at source at a 50 per cent rate, from the first dollar of other income (but not exceeding earnings covered by the GIS income test), and with the GIS payable in full.

'In Table 2, notice that the end results are exactly the same, whether (A) at present, or (B) under a unified tax-transfer system:

TABLE 2

Monthly Income - April-May-June 1983

Item	(A) At Present ..... Separate Systems	(B) Initial Illustration ..... Unified Tax-Transfer System
Private income	+400.00	+400.00
Less: income tax	Nil	-200.00
Old-age security	+254.13	+254.13
Guaranteed income supplement	+ 55.13	+255.13
NET INCOME	709.26	709.26

'Equally, both at present and under a unified tax-transfer system, the private income of $400 a month is increased by $309.26 up to a total net income of $709.26. Thus, both ways are equally selective. That is, both ways are equally targetted towards need. Also, both ways provide an equal 50 per cent incentive to work and to save.

Differences

'There are differences, however. Referring not only to the example immediately above but to the totality of government financial aid measures as a whole, some of these differences are touched on in summary form in Table 3:

TABLE 3

Nine Points to Watch

Question	Separate Systems	Unified Tax-Transfer System
1. Stigma Avoided?	No	Yes
2. 100 Per Cent Take-Up?	No	Yes
3. Monthly Payment Readily Possible?	Sometimes No	Yes
4. Immediate Response to Income Fluctuation?	No	Yes
5. Horizontal Equity?	Not at Present	Possible in Future
6. Vertical Equity?	Not at Present	Possible in Future
7. Administration Minimized - for Governments?	No	Yes
8. Administration Minimized - for Individuals?	No	Yes
9. 'Reverse' Selectivity Readily Eliminated?	No	Yes'

Ending Regressivity

Having looked at a single example of the mechanics of a unified tax-transfer system, now consider such a unified system but this time with the regressivity of taxation ended.

Suppose that it was decided that there would be no increase in the average rate of taxation of any Senior Canadian.

Suppose, however, that those with the lowest incomes and with medium incomes would have their average rates of taxation reduced - but only to the minimum extent necessary to convert the pattern of taxation from being regressive into being progressive.

In the particular example being discussed of a certain Ontario Senior Canadian married couple (see Appendix B), there would therefore be a flat, equal rate of taxation of 40.63% on all 'other' income, from the first dollar up to $41,248.

If this were done, there need be no change in the net spendable income at the two extremes. Those with zero 'other' income would have the same total subsidisation as received at present. Those with 'other' income at least equal to $41,248 would also have the same net spendable income as at present.

However, all those in between - i.e. those with smaller or moderate 'other' incomes - would receive an increase in their spendable income - to a lesser or to a larger degree, but only to the extent necessitated by the

requirement that the taxation of incomes of Senior Canadians no longer be regressive.

See the sample illustration in Table 8.

TABLE 8

SPENDABLE 'OTHER' INCOME

SENIOR CANADIANS - TYPICAL MARRIED COUPLE - ONTARIO*

Integrated tax-transfer system - initial tax rate 40.63%					
'Other' income (1)	Increase in OAS (2)	Dollars of taxation (3)	Spendable Income = (1)+(2)-(3) (4)	At present Spendable income (5)	Increase in spendable income = (4)-(5) (6)
Nil	$6,666	Nil	$ 6,666	$ 6,666	Nil
$ 3,844	6,666	$ 1,562	8,948	6,666	+$2,282
9,488	6,666	3,855	12,299	9,488	+2,811
10,224	6,666	4,154	12,736	10,224	+2,512
10,416	6,666	4,232	12,850	10,275	+2,575
10,594	6,666	4,304	12,956	10,411	+2,545
12,952	6,666	5,262	14,356	12,176	+2,180
15,310	6,666	6,220	15,756	13,905	+1,851
20,026	6,666	8,137	18,555	17,295	+1,260
24,742	6,666	10,053	21,355	20,614	+741
29,458	6,666	11,969	24,155	23,726	+429
41,248	6,666	16,760	31,154	31,154	Nil
64,828	6,666	27,230	44,264	44,264	Nil

* For details underlying Table 8, see Appendix B.

Clearly, even just a quick glance at column (6) on the right-hand side of Table 8, shows that such a change by itself alone would entail a considerable increase in Government expenditures for Senior Canadians with moderate 'other' incomes.

If the relatively high, flat, initial tax rate of 40.63 per cent were reduced, to say 35 per cent, the cost would be substantially greater again, as can be deduced from column (6) on the right-hand side of Table 8.

TABLE 9

SPENDABLE 'OTHER' INCOME

SENIOR CANADIANS - TYPICAL MARRIED COUPLE - ONTARIO*

Integrated tax-transfer system - initial tax rate 35.00%					
'Other' income (1)	Increase in OAS (2)	Dollars of taxation (3)	Spendable Income = (1)+(2)-(3) (4)	At present Spendable income (5)	Increase in spendable income = (4)-(5) (6)
Nil	$6,666	Nil	$ 6,666	$ 6,666	Nil
$ 3,844	6,666	$ 1,345	9,165	6,666	+$2,499
9,488	6,666	3,321	12,833	9,488	+3,345
10,224	6,666	3,578	13,312	10,224	+3,088
10,416	6,666	3,646	13,436	10,275	+3,161
10,594	6,666	3,708	13,552	10,411	+3,141
12,952	6,666	4,533	15,085	12,176	+2,909
15,310	6,666	5,359	16,617	13,905	+2,712
20,026	6,666	7,009	19,683	17,295	+2,388
24,742	6,666	8,660	22,748	20,614	+2,134
29,458	6,666	10,310	25,814	23,726	+2,088
41,248	6,666	14,672	33,242	31,154	+2,088
64,828	6,666	25,142	46,352	44,264	+2,088

* For details underlying Table 9, see Appendix B.

Balancing the Books

To offset the substantial costs of eliminating regressivity from the taxation of Senior Canadians, four areas deserve consideration:

1. the definition of adequacy (see Chapter 7)
2. the targetting of housing assistance (see Chapter 8)
3. the age of normal retirement (see Chapter 9)
4. the setting of income replacement objectives (see Chapter 10).

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SUMMARY

1. The income tax system and the income security system should be treated as *one*, single system - i.e., a *unified* tax-transfer system.
2. Regressivity should be eliminated from the taxation of Senior Canadians, with the substantial costs of so doing appropriately offset.

7
ADEQUACY

There is much talk of across-the-board levelling up of the minimum monthly income guaranteed to a Senior Canadian by OAS/GIS, so as to reach an 'urban poverty line'.

So doing would be needlessly costly, since many Senior Canadians live outside the larger cities and many have lesser housing costs (see Chapter 8).

More fundamentally, mechanical implementation of such 'poverty lines' would create a serious imbalance unduly favouring Senior Canadians, to the detriment of many working Canadians, e.g., faced with the costs of raising young children, accumulating furniture, retiring the mortgage, etc.

Accordingly, rather than blindly adopting theoretical poverty lines, spokespersons for the private sector in the national pension debate appear to be advocating that the minimum incomes of Senior Canadians should be kept at least equal to an acceptable minimum standard. Even with no other sources of income, as a minimum the OAS, GIS and provincial supplements should be sufficient to provide housing, food, clothing, and the cost of personal expenses, having due regard to the standard of living achieved by typical working Canadians.

7

SUMMARY

1. Theoretical poverty lines are insufficiently in touch with the real world.
2. With due regard to the standard of living achieved by typical working Canadians, the total of the OAS, the GIS, and the provincial supplements should be sufficient to provide housing, food, clothing, and the cost of personal expenses.

8

HOUSING

The additional costs would be large enough, for any one of the following taken singly:

1. making minimum government pensions adequate
2. eliminating inequities from income subsidies
3. eliminating inequities from income taxation.

The additional costs of doing all three at once - so imperative if there is truly to be real pension 'reform' - would be huge.

Differential Housing Costs

One powerful lever for helping to keep government pension costs within tolerable limits for Canadians as a whole, would be 'targetting' varying amounts of monthly cash income to individual Senior Canadians in relation to their differential housing costs, i.e., (A) as to whether they live:

- rurally
- in towns
- in cities

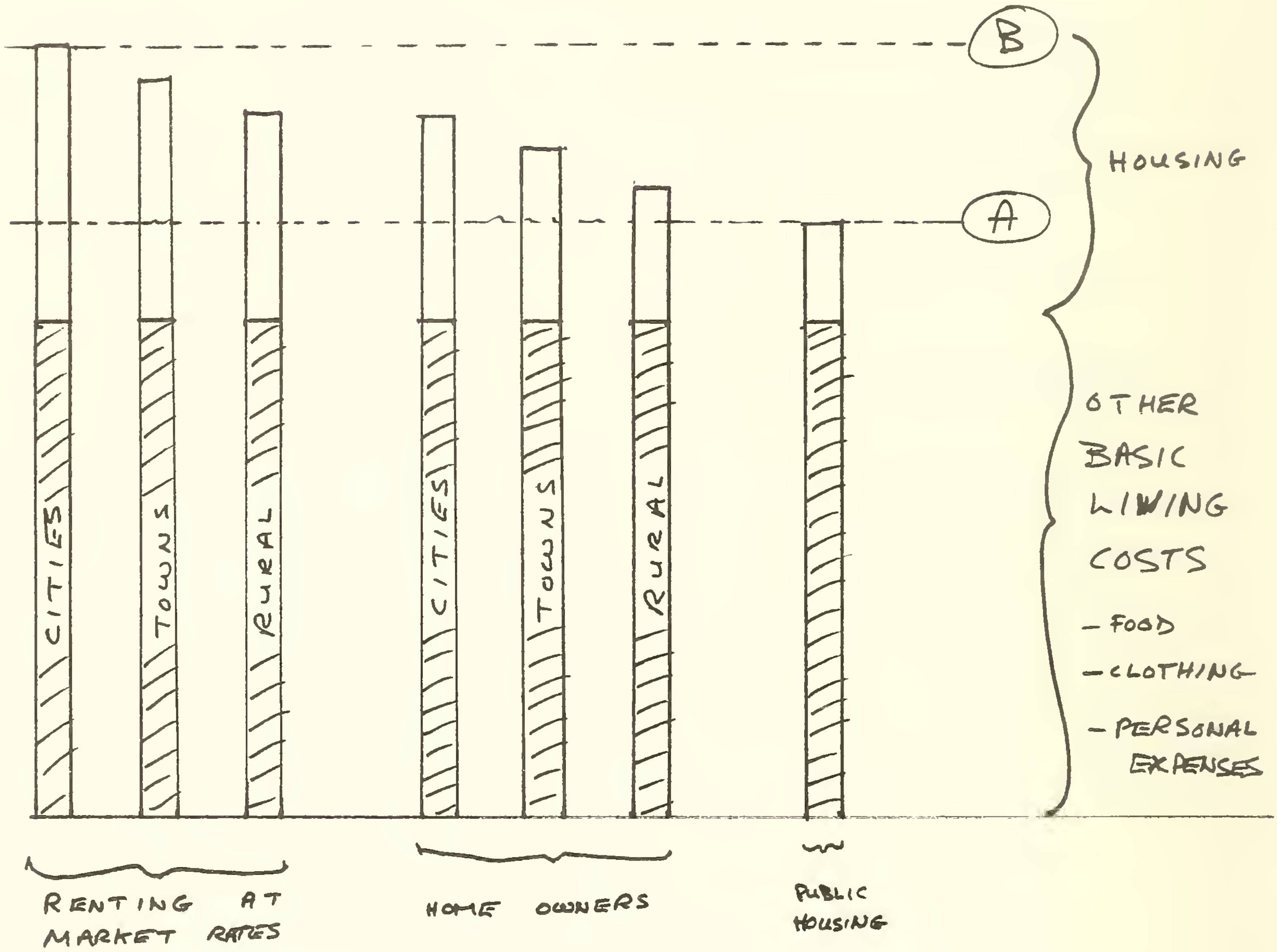
and (B) as to whether they live in:

- subsidised public housing
- homes of their own
- apartments rented at market rates.

While housing costs vary significantly as touched on above, as a general rule there is much less variation across Canada as to the monthly cash needed for other basic living costs, i.e.

- food
- clothing
- personal expenses.

Thus, very schematically, for a single Senior Canadian, we could expect to find his/her monthly cash requirements to be somewhat as follows:



If cash is paid out equally to all - i.e. as at present with our flat minimum OAS/GIS formula applicable throughout Canada, regardless of the actual differential housing costs - then one of two things happens:

(A) Suppose everyone receives just enough to cover basic living costs plus the net rent payable for public housing. The monthly incomes will not be enough for those with higher housing costs, including for example those renting at market rates. The latter will have too little money left to maintain an acceptable minimum standard of food, clothing and personal expenses.

(B) On the other hand, suppose everyone receives a monthly income that is large enough to meet the needs of Senior Canadian renting a city apartment at market rates. Then income security costs to Canadians as a whole will be needlessly high, since all Senior Canadians other than city market-rate apartment dwellers will be paid more than is required to maintain an acceptable minimum standard.

As a first step towards efficient and effective program design and delivery, consider how the housing component of OAS/GIS may be identified and broken out.

What follows is not intended to be definitive as to dollar amounts. Rather, it is purely illustrative.

In each of July-August-September 1983, we had:

		Single	Married
OAS		$256.67	$256.67
OAS		-	256.67
GIS (maximum)		257.68	198.67
GIS (maximum)		-	198.67
	TOTALS	$514.35	$910.68

The single total of $514.35 was only 56% of the married total of $910.68.

Suppose, purely for purposes of illustration, our elected representatives decide that 60 per cent would be more appropriate. The single total would then be $546.41, i.e. an increase of $32.06.

Further, and again purely for purposes of illustration, under a unified tax-transfer system, the disbursements could be re-arranged thus:

		Single	Married
Combined OAS/GIS		$364.27	$364.27
Combined OAS/GIS		-	364.27
Monthly Shelter Allowance		182.14	182.14
	TOTALS	$546.41	$910.68

Note, in the above illustration:

1. The monthly amounts of combined OAS/GIS would be equal, whether the individual be single or married. Thus, there would no longer be 'a penalty on marriage'.
2. Having broken out the cost of housing separately, targetting could now be improved still further if, for example, the monthly shelter allowance were varied as between market-rate renters vs. home owners vs. public housing renters, and as between cities vs. towns vs. rural.

Provincial Administration?

The administrative records and the practical expertise for varying monthly income security disbursements in reasonably and acceptably close relation to actual housing costs, exist most obviously at the provincial level.

Witness various measures already in effect, for example in:

- Alberta
- Ontario
- Quebec.

In Alberta, pensioners who are renters receive an annual grant, 'targetted' directly to them (i.e. and not to home owners).

In Ontario, the Tax Grants happen to be equal - at $500 a year - to many renters and many home owners alike. However, with the existing mechanisms Ontario has already put in place, it would be readily possible to differentiate future increases in Tax Grants appropriately in favour of renters.

In Quebec, 'Logirente' is a first step in recognizing that, as between two neighbours in identical housing and on identical incomes, the out-of-pocket burden is greater for the renter than it is for the home owner.

The 'Logirente' payments, accordingly could be readily tilted more and more in favour of the renter.

Subsidized housing - in Ontario

Page 5 of Budget Paper B to the Ontario Budget 1980, stated:

'... Selective benefits are provided to some pensioners through the subsidization of senior citizen housing. ...[the table below] summarizes the major programs.

Cost Relief for Ontario Pensioners in 1979-80

	Beneficiaries (000)	Cost ($ million)
Free OHIP	850*	205
Free Prescription Drugs	800	105
Subsidized Nursing Homes**	21	150
Subsidized Homes for the Aged**	26	125
Subsidized Housing**	67	115
Total Cost		700

Source: Ontario Treasury estimates.
* Includes dependants.
** Cost shared with the federal government.
Note: Subsidized housing does not include estimates for senior citizens living outside of Metropolitan Toronto receiving the rent-geared-to-income supplement.

Per the last line of the above table, note that 67,000 Beneficiaries benefit from $115,000,000 of 'subsidization' annually. That is, on average, each Beneficiary receives just over $1,700 of subsidization each and every year via public housing for the elderly.

Note further:

1. Since this subsidization is necessarily restricted to those who (a) happen to live in communities where public housing for the elderly is available and (b) happen to have applied for it, it is by no means the case that these particular 67,000 Beneficiaries are the Senior Canadians in Ontario with the lowest 67,000 incomes - many will be, but at least some will not. That is, some of the lowest incomes will be unsubsidized, while some subsidies will go to some people who do not have the lowest incomes.

2. In any event, there is an abrupt discontinuity between the 67,000 who are subsidized vs. those who are not. Cross the boundary from being, say, '#66,999' and subsidized, over to being '#67,001' and not subsidized, and abruptly your subsidization drops (on average) $1,700 a year.

Economic Council of Canada

Note: The above was drafted in Setpember, 1983. Then, in mid-October, 1983, the Economic Council of Canada published its Twentieth Annual Review, 1983, 'On the Mend'.

Here is how the Economic Council of Canada views public housing (including for pensions) vs. shelter allowances:

'Whatever the merits of the CMHC's present social housing programs on other grounds, they are not an adequate vehicle for assistance to those experiencing genuine housing need.

'... while they are not a panacea, shelter allowance programs, in our view and given the present environment of limited government resources, offer important advantages. Given the high cost to government of low-income Section 56.1 units already in place (as well as that of public housing), compared with the payments made under shelter allowance programs, and given the variability of rents from one location to another (because of partial rent controls and varying rates of inflation), shelter allowance schemes offer more flexibility in dealing with inadequate shelter situations and could potentially cover a much larger percentage of persons in need than do the present Section 56.1 programs. We believe that careful consideration should be given to them in the current review of the CMHC's social housing strategy.'

In my remarks above, three Provinces are given initial mention to illustrate the administrative feasability of provincial shelter allowances. The Economic Council mentions a further four Provinces which established shelter allowance programs in the years shown:

1977 - British Columbia
1978 - New Brunswick
1979 - Manitoba
1981 - Nova Scotia.

8

SUMMARY

1. Housing costs vary, i.e., as between
   - rural
   - towns
   - citites

   and as between
   - subsidised public housing
   - homes of their own
   - apartments rented at market rates.
2. The housing component of OAS/GIS could be broken out, and differentiated by the Provinces, and hence 'targetted' to needs, for maximum efficiency and effectiveness.
3. At least seven Provinces are known to have administrative mechanisms already in place which do indeed deliver 'targetted' shelter allowances, or which could be simply adjusted to do so.
4. The balance of OAS/GIS - for food, clothing and personal expenses - could be equal and uniform for all.

THE AGE OF RETIREMENT

The fulcrum of all financial planning is the age of retirement. Lower the age of retirement even just a little, and either:

- for an equal cost, benefits drop off sharply; or
- with benefits kept intact, costs go up sharply.

Alternatively, increase the age of retirement even just a little, and either:

- for an equal cost, benefits go up sharply; or
- with benefits kept unchanged, costs drop off sharply.

For example, for male lives, under a non-contributory pension plan with no death benefits, the following results were indicated by a paper prepared by the 1982 Society of Actuaries' Pension Committee, where retirement is postponed from the normal age of 65 to the age shown:

	Relative Cost		Equivalent Pension	
Age at Retirement	6% Interest	8% Interest	6% Interest	8% Interest
65	1.0000	1.0000	$100	$100
66	.8940	.8805	$112	$114
67	.7966	.7728	$126	$129
68	.7033	.6759	$142	$148
69	.6257	.5889	$160	$170
70	.5512	.5110	$181	$196

In other words, if interest is earned, say, at a rate of 6 per cent throughout retirement, then the funds on hand at age 65 to pay everyone a non-contributory pension from that age of $100 a month will - on their own, without any further contributions - provide $181 a month if retirement is delayed to age 70.

By itself, 6 per cent interest compounded over 5 years will only increase $100 up to $134. Therefore, there is clearly more involved than simply investing the funds for a further 5 years. In fact, what also happens is that 'mortality' comes into play in these two directions:

1. at age 70, people have fewer years of retirement ahead of them than at age 65; and
2. of any group of lives at age 65, some will die before age 70, so that the total population is smaller at 70 than at 65.

Conversely, of course, lowering the starting age of pensions is more costly than you might imagine from just looking at compound interest tables alone. Here there is, again, a double 'mortality' impact, only this time it is doubly adverse in financial terms, thus:

1. at age 60, people have more years of retirement ahead of them than at age 65; and
2. in any group of lives, the total population is larger at 60 than at 65, since some will die in those 5 years.

<u>Selected reports</u>

For further detailed discussion, see:

1. The 1950 Report of the Joint Committee of the Senate and House of Commons on Old Age Security: The King's Printer (see pages 101, 102, 107 and 108).
2. The 1961 Second Report of the Ontario Committee on Portable Pensions: Government of Ontario (see pages 84, 85, 86 and 87).
3. 1982 Discussion Paper, 'Developing a Pension Policy for the Future': Province of British Columbia (see pages 5, 17, 18, 19, 23, 28 and 29).

Generally speaking, all three of these reports shown a keen awareness that if priority is given to both (a) adequacy of pension benefits and (b) cost control, then it makes sense to ponder carefully the powerful assistance that can be rendered by (c) raising the age of retirement.

Some history

It is important to note that there is nothing 'scientific' about age 65 currently being a common age of retirement, including for the OAS, the GIS, the CPP/QPP, and counterpart provincial supplements.

More specifically, age 65 has no 'actuarial' justification whatsoever. Rather, age 65 is no more nor less than a widespread 'habit'.

When government pensions were first established for the general population - in Germany, in the late 19th Century - age 70 was adopted as the initial age of retirement, simply because at that time few workers were expected to survive for very long after age 70 and hence the total cost would be held down. The subsequent lowering of that age of retirement to 65 was not (to our knowledge) based on any 'evidence' of a scientific or actuarial nature - rather, it was an arbitrary choice.

When, in the 1930's, the United States established its Social Security System, there was a general surmise that age 60 would be too costly, but that age 70 would not contribute enough to reducing unemployment, so age 65 was an off-the-top-of-the-head compromise. Rather recently, the pressures of (a) escalating costs and (b) popular attachment to existing benefit levels, have resulted in the U.S. Congress raising the age of retirement first to 66, and then to 67, but in each case phased in over a period of years.

Here in Canada, the 1950 Joint Committee of the Senate and House of Commons on Old Age Security made a worthy attempt to select an age of retirement, deliberately and consciously. They discussed:

- adequacy of pension benefits
- total costs to the taxpayers
- the physical health and the mental health of individuals, which often (but not always) benefit from more employment rather than less
- national Canadian 'economic progress and prosperity'.

Not only did this 1950 Joint Committee turn its back on age 65 (and on age 60, for that matter), in favour of age 70 initially, but also it advocated that 'in the years ahead' people should, if anything, work more beyond age 70 rather than less.

When some years later (1966-1970) the age of retirement was lowered under OAS from 70 down to age 65, no known justification was ever pre-

sented, neither federally nor in Quebec, by way of extensive scientific or actuarial justification. (As noted above, the 1961 Second Report of the Ontario Committee on Portable Pensions, dwelt more on the advantages of later retirement which, however, to have been overlooked in the political rush to implement the CPP/QPP, and to make OAS available at age 65.)

Thus, there really is no hard and fast justification for age 65 being of such common application.

A fresh look

A further powerful way of keeping government income security costs within limits tolerable to Canadians as a whole, would be an increase in the age of normal retirement in effect under OAS, the GIS, the CPP/QPP and provincial supplements, i.e. an increase from age 65 up to (say) age 66, or 67, or 68.

Later retirement may also have appreciable advantages for many individual Senior Canadians regarding health and satisfaction, and indeed as well for our national prosperity.

Certainly, as acknowledge by Clare, it is not merely a financial matter. It is also very much a question of the health and social well-being of the individual. Further, it is an important question for employers, as the 1982 B.C. Discussion Paper states:

> 'It has been argued, however, that a negative factor associated with permitting later retirement is the possibility that some organization costs might be involved because of a slowdown in the flow of promotions.' (p. 29)

Nevertheless, the magnitude of the additional leverage obtained from shifting the retirement age 'fulcrum' is so great, and so potentially beneficial to all concerned, that the subject of deliberately and consciously selecting the age of retirement deserves major attention in any pension reform study that is to be worthy of being truly labelled 'reform'.

9
SUMMARY

1. The age of normal retirement is a major element in the design of any pension scheme.
2. Achieveing adequate government pensions for all, with equitable taxation of all private income of Senior Canadians, with tolerable total tax burdens on working Canadians, will be more readily possible if the age of normal retirement for OAS, the GIS, the CPP/QPP, and provincial supplements is increased appropriately, over time.

10

INCOME RELACEMENT

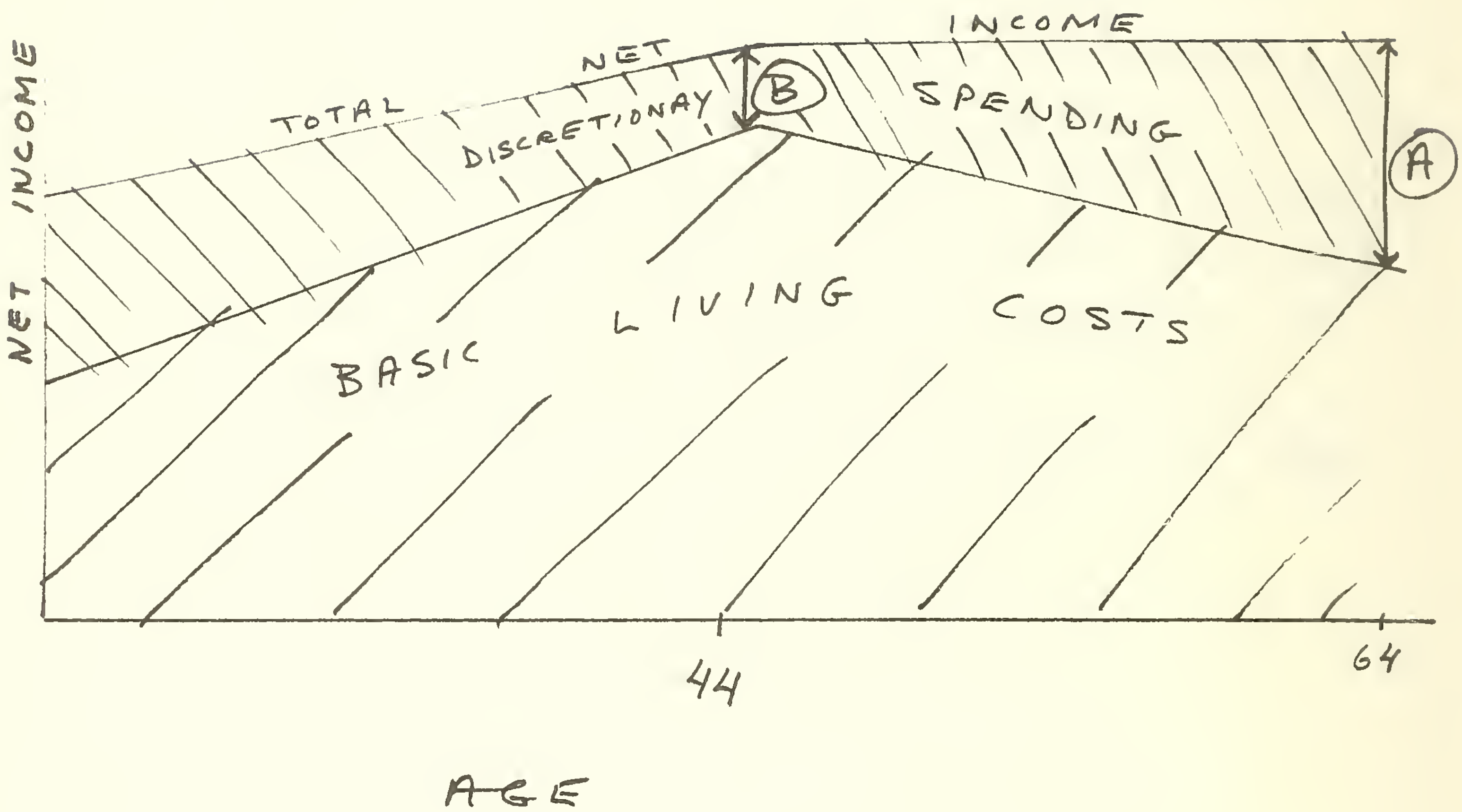
Over and above ensuring that all Senior Canadians enjoy an adequate minimum standard of living including suitable housing, there is the further question of middle-income and higher-income people having appropriately higher retirement incomes.

This is the question of 'income replacement'.

However, when it comes to setting an appropriate 'net replacement ratio target', care is needed.

It is not appropriate to attach undue weight to a 'single point in time' comparison between (a) net spendable income in retirement at age 66, vs. (b) net spendable income while working at age 64. Rather, what is needed is a realistic 'career' comparison.

Consider one occupational category, e.g. bus drivers, and see how the discretionary income available for personal spending varies over a typical career. Schematically we have:


NET INCOME
TOTAL NET INCOME
DISCRETIONAY SPENDING
B
A
BASIC LIVING COSTS
44
64
AGE

At age 65, the amount of net income freed up for discretionary spending, i.e. 'A', is typically significantly greater than the corresponding amount at mid-career, at age 44 say, i.e. 'B'. This is because at age 64 one has finished raising children, paying off the mortgage, etc.

If new legislation were enacted to mandate that the net spending power of those aged 66 and over be on a par with that of those aged 64, then substantial additional sums would have to be taken away from working Canadians, including the one aged 44. The imbalance in favour of the one aged 66 would be beyond any real political justification.

Mechanics

If our elected representatives still decide that there is a need for mandating the taking away of more pension contributions from working Canadians to achieve greater 'income replacement', it should not be done by expanding the CPP/QPP, since their earnings-related benefit formula inevitably gives rise to 'upside-down windfalls' (see Chapters 1 and 2).

Rather, mandatory supplemental retirement savings should be on a money-purchase basis, e.g. through locked-in RRSP's. As advocated generally by the Vancouver Board of Trade, existing employment pension plans could be modified to satisfy such 'income replacement' mandatory minimum requirements.

Those not members of employment pension plans could contribute voluntarily to locked-in RRSP's, in at least the required minimum amounts. Any one individual reporting less than the required contributions on his federal income tax return, could have the difference taxed away by Revenue Canada, and deposited in his name in a locked-in RRSP administered by a private sector entity.

10
SUMMARY

1. Net replacement ratio comparisons should be on a 'career' basis.
2. The CPP/QPP should not be increased, since their earnings-related benefit formula inevitably gives rise to 'upside-down windfalls'.
3. Mandatory supplemental retirement savings (if really necessary), should basically be via private sector locked-in RRSP's.
4. Revenue Canada could assist in channelling contributions, where necessary.
5. Existing employment pension plans could be adopted to cover off the mandatory minimum supplemental retirement savings, for plan members.

11
FIRST STEPS

Canadian taxpayers are already handing over annually very substantial sums of dollars towards improved income security of Senior Canadians.

The trouble is, these tax monies are not being spent as well as they could be. Some needs of some Senior Canadians are not now being covered. True, in some cases, eligible Senior Canadians are not applying for benefits available to them, but even so the fact is that their needs remain uncovered on account of 'faulty design'.

The weaknesses and inefficiencies of the present arrangements, of all kinds, foster demands for more and more spending, at more and more cost to Canadian taxpayers.

The alternative would be a <u>rationalisation</u> of <u>existing</u> tax monies - using the <u>mechanics</u> suggested in this present discussion.

The monies already being collected from Canadian taxpayers and ear-marked for Senior Canadians should be used more wisely.

The needs of Senior Canadians could then be satisfied better - at no more cost to Canadian taxpayers.

Step by Step

It would be mathematically possible simply to turn over a new leaf, all at once so to speak, eliminating all unfairness at one full swoop. However, total reform done so abruptly would be dislocating and unsettling both for hundreads of thousands of Senior Canadians and for millions of working Canadians looking ahead to retirement.

Certaintly we first need a full enough grasp of the nature and the total extent of the existing inequities, i.e.

- subsidies are too often 'upside-down windfalls', giving more not-paid-for help to high-income Senior Canadians than to low-income Senior Canadians.
- the taxation of income is regressive, with many higher-income Senior Canadians paying less in taxes of all kinds, on average as a percentage of total income, than lower-income Senior Canadians.

Then, our elected representatives - certainly the Parliamentary Task Force on Pension Reform, but also including our federal and provincial Governments - will need to sort out a series of first steps.

How much can be done, and how soon? Subject to more detailed testing out, likely questions and answers appear to be as follows.

CPP/QPP 'Upside-Down Windfalls'

The 'upside-down windfalls' of the CPP/QPP could be (in part) counteracted and neutralized as follows:

- raise the GIS tax-back rate significantly above 50 per cent regarding CPP/QPP benefits - only and exclusively regarding CPP/QPP benefits.

That is, CPP/QPP benefits taken into the GIS income test could be 'grossed up', by a factor greater than 1.

As discussed above, the GIS tax-back rate for income other-than - CPP/QPP needs to be reduced, from 50 per cent down to (say) 35 per cent, or even 30 per cent, to provide a fair incentive to contribute to RRSP's and to RPA's.

Suppose, for example, that for all income other-than-CPP/QPP, the GIS tax-back rate were 35 per cent. Then, if the CPP/QPP benefits were (as just one hypotehtical illustration) grossed-up two-and-a-half times currently before being taken into the GIS income test, they would be effectively taxed back at a rate of 87.5 per cent (where 2½ times 35 per cent equals 87.5 per cent).

In round numbers, for the individuals affected, such two-and-a-half times grossing up of CPP/QPP benefits would closely cancel out the effect of the CPP/QPP 'upside-down windfalls', which are in the area of 84 per cent to 90 per cent currently.

Of course, the remaining 12.5 per cent of CPP/QPP benefits would then effectively be free of 'taxation of income', although private pension

income would be 'taxed' 35 per cent by the GIS tax-back. Accordingly, a case could be made for grossing up CPP/QPP benefits somewhat more than two-and-a-half times.

11
SUMMARY

1Q. How do we stop matters from going from bad to worse?

A. Stop CPP/QPP 'upside-down windfalls' from getting any bigger:

- do not increase the CPP/QPP retirement pension benefit percentage above 25 per cent
- do not make catch-up increases in the YMPE; rather, freeze the YMPE.

2Q. How can subsidy unfairness be reduced?

A. While lowering the GIS tax-back rate on 'other' income in general, nevertheless raise the GIS tax-back rate significantly above 50 per cent just regarding CPP/QPP benefits. Raise rents on public housing for Senior Canadians to market levels which fairly reflect all costs including full financing costs.

3Q. What else can be done to free up money to pay for "adequacy", and to reduce taxation unfairness?

A. The age of normal retirement for the OAS, the GIS, the CPP/QPP, and provincial supplements could be raised above 65 - gradually, and over time perhaps.

4Q. What can be done so that the estimated 184,000 eligibles missing out on the GIS do in fact receive it, so that the perceived 'stigma' of the GIS disappears, and so that problems of GIS recipients caused whenever their incomes fluctuate, are eliminated?

A. For those eligible for both OAS and the GIS (i.e. for Canadian residents), merge the OAS and the GIS into a single plan payable universally, with total OAS/GIS benefits then split between (a) an equal benefit per person adequately covering food, clothing, and personal expenses, and, (b) an appropriate monthly shelter allowance per household.

5Q. How can the monthly shelter allowance achieve optimum efficiency, effectiveness and value for money?

A. Administered provincially, the amount of the monthly shelter allowance per household could be varied to reflect reasonably the major variations in costs as between renters vs. home owners, and as between rural vs. urban, etc.

6Q. How can taxation unfairness be reduced?

A. The combined OAS/GIS payment including the monthly shelter allowance, would not be taxable, and all other income would be taxable from the first dollar onwards, generally speaking with no personal exemptions and no pension deductions, etc. Income tax could be readily deducted at source, fully covering all taxes due from most Senior Canadians.

7Q. What are the basic, fundamental policy choices?

A. Political decisions would be needed as to (a) 'adequacy', e.g. by how much income should be increased for a single Senior Canadian renting at market rates, and (b) 'taxation', i.e. the rate of tax on the first dollar of other income (perhaps in the area of 40 per cent initially, but lowered in due course?).

8Q. What are the longer-term needs?

A. Reducing the rate of tax on the first dollar of other income down to comparability with typical top marginal rates when working, such as 35 per cent/30 per cent or even lower.

APPENDIX A

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APPENDIX B

DETAILS UNDERLYING THE ILLUSTRATIONS

The patterns of taxation and the patterns of subsidy illustrated in the paper are not isolated exceptions.

Broadly and in general, they are indeed characteristic of the situations in which all Senior Canadians find themselves in 1983 whether married or single, whether in Nova Scotia, or Ontario, or elsewhere.

Specific Illustrations

The specific illustrations consider the following Senior Canadians:

- They are single, or married, as shown in the text.
- They live in Nova Scotia, or Ontario.
- All attained age 65 in January 1983, and all 'assumed' to receive Old Age Security (OAS) for a full 12 months in 1983 (to give a full annual income).
- 'Other' income is the total income of the couple, exclusive of all OAS payments and all GIS payments and also exclusive of Ontario Tax Grants.
- Where 'other' income exceeds $4,000 a year - one spouse receives $2,000 of which $1,000 is interest income and the $1,000 balance is pension income (for income tax purposes) - the other spouse receives the balance of 'other' income, and this other spouse's balance of income includes a further $1,000 of interest income and a further $1,000 of pension income.
- The spouse receiving the balance of 'other' income claims a standard $100 deduction against taxable income.
- For simplicity, it is assumed that the reductions of the Federal Guaranteed Income Supplement (the GIS) equal a 'steady' 50 per cent of 'other' income.

- For simplicity, it is likewise assumed that the Ontario Guaranteed Annual Income System (GAINS) reductions equal an additional 'steady' 50 per cent of 'other' income.
- Since the calculations were computed in the summer of 1983, benefits for the fourth quarter were 'assumed' to increase over those of the third quarter, at the same compounded rate of increase that benefits for the third quarter increased over those of the second quarter.
- Since it is temporary (i.e. only for 1983 and 1984), the Ontario Social Services Maintenance Tax which adds a personal income tax surcharge, is not included.